



Our Ref.: CJ/S&R/UKCMA

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By email to: [statutoryauditmarket@cma.gov.uk](mailto:statutoryauditmarket@cma.gov.uk)

Statutory audit market study  
Competition and Markets Authority  
7<sup>th</sup> Floor  
Victoria House  
37 Southampton Row  
London  
WC1B 4AD

Dear Sirs,

### **Statutory audit services market study – Update Paper**

The Hong Kong Institute of Certified Public Accountants (the Institute) is the only statutory licensing body of accountants in Hong Kong responsible for the professional training, development and regulation of the accountancy profession. The Institute sets auditing and assurance standards, ethical standards and financial reporting standards in Hong Kong. The Institute is committed to ensuring that audit quality is maintained at the highest standards and therefore welcomes initiatives that share this aim.

Thank you for publishing the very detailed and thorough update paper on 18 December 2018. As mentioned in our previous correspondence the Institute has an interest in your work, being mindful of the potential international ramifications. Important national initiatives and best practice examples tend to be "exported" as no single jurisdiction operates in isolation of without reference to its peers. The recognition of the value of audit to capital markets is important and audit quality remains a legitimate topic of interest for all market participants. Accordingly the comments below, that have been developed by management with input from relevant committees of the Institute, try to address the proposed remedies on matters of principle and how consequences of implementation of remedies are likely to affect markets in general. We do not comment on matters specific to the UK FTSE 350 audit market.

#### ***Regulatory scrutiny of audit committees***

We concur that the potential remedy of making auditor appointment independent from the company should not be pursued at this point in time. We agree that steps to strengthen the role and effectiveness of Audit Committees would be an important and welcome development as the important role of Audit Committees under the current regime is not consistently understood or implemented. Whether the regulator of listed company auditors is the most appropriate body to exercise direct regulatory scrutiny of Audit Committees should be further considered. Given the potential impact by actions of the Audit Committee on quality of audit there is logic behind the proposal. However, consideration should be given to how such an arrangement would fit with the responsibilities of other market regulators.



### ***Mandatory joint audits***

The CMA proposals recognize that there are practical challenges to this proposal but do offer solutions e.g. tendering and appointment for each audit firm to be staggered to ensure continuity of knowledge and experience. We see this remedy as primarily a market remedy, providing a way in which challenger firms can break into the FTSE 350 audit market. The CMA does put forward arguments on how it could also enhance audit quality, but the report itself acknowledges that evidence on joint audits effect on audit quality is mixed. The proposals include suggestions on how to encourage challenger firms to join the market and develop capacity, skills and expertise – such as starting with a relatively small share of the joint audit which will increase over time. In our view not all challenger firms will have the appetite for this change and we note that in the UK Grant Thornton has been reported as saying it is not interested in expanding into this market.

### ***Market share cap***

We concur that this remedy should not be pursued.

### ***Additional measures to support challenger firms***

We note that the CMA proposes to further explore additional measures including ease of movement of staff between firms and access to technology. If practical and non-intrusive solutions to develop audit quality across a wider spectrum of firms can be found we would be willing to consider but in principle we do not support regulatory manipulation of the market.

### ***Market resilience***

The failure of any one of the Big4, or challenger firms, in a major jurisdiction could have serious implications on the international network and consequently other jurisdictions. We support consideration of developing proposals to strengthen market resilience.

### ***Full structural or operational split between audit and non-audit services***

We recognize that this area has been subject to discussion for many years and standards and regulations have been changed to address the potential implications to auditor independence by the provision of non-audit services. We do not concur with the CMA conclusion that "we do not believe the current framework for managing non-audit services conflicts is sufficient to focus auditor's incentives on high quality audits."

We are concerned that separation to the extent proposed would have an adverse, or at least not a positive, effect on audit quality. We also believe that there are potential negative effects that need further consideration. The CMA recognizes that there could be negative effects, saying "a restriction on non-audit services that would exclude Challenger firms from audit tender processes runs counter to our objectives."

### ***Peer review***

Whilst we understand the attractions of adding another layer of "real time" review to the audit process we do not believe that the proposals are practical. Anything other than a superficial exercise would be costly and time consuming and would only lengthen the audit process. A high level review, possibly perceived to be "lightweight" would add no benefit.

As well as liability concerns around the role of the peer reviewer there would be issues about who could fulfill the role in a market where the number of participants is already low and conflicts are increasingly placing limits of the work that firms and individuals can undertake.

If there is a case for real time reviews of high risk audits then this step should be undertaken by the regulatory authority directly as part of its regulatory activities and not delegated to a third party.



In the update paper the CMA recognises that market remedies and consequential changes to the UK audit market need to be considered in conjunction with the recommendations of the Kingman report on the effectiveness of the Financial Reporting Council, the regulator of public interest entity auditors. We strongly support a fully joined up approach and look forward with interest to following developments.

I trust that the above comments are of assistance to you. If you require any clarification on our comments, please do not hesitate to contact me by email [ ] or telephone (direct line [ ])

Yours faithfully,

Chris Joy  
Executive Director

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