



London, 30 November 2011

In a follow up to its 30 September letter to the UK's European Commissioner Cathy Ashton setting out views on the proposed reform of the external audit market, the Hundred Group responds to the draft regulations announced earlier today by Internal Markets Commissioner Michel Barnier.

The draft regulations abandon previous proposals which required mandatory joint audits, however continue to contain radical proposals to legislate for mandatory external audit tendering, the creation of specialist audit firms and a widespread prohibition on non audit services. They also tighten previous proposals on mandatory external audit firm rotation, reducing the maximum engagement period to six, from nine, years.

The Hundred Group today also reports on the results of a survey undertaken amongst its membership on reform of the external audit market. Survey respondents unanimously rejected the concept of mandatory audit firm rotation and mandatory joint audits. As regards audit tendering, respondents indicated a clear preference for proceeding on a 'comply or explain' basis, with less than 15% supporting a mandatory approach based on a legislated time period.

Commenting on the European proposals and the survey results, Andy Halford, Chairman of the Hundred Group said:

"We are pleased that the proposals issued today reflect the Hundred Group's previous opposition to mandatory joint audits. However the draft regulations on mandatory audit firm rotation, audit tendering, the creation of audit only firms and a widespread prohibition on non audit services will still have very significant and profound implications for the way audits are conducted. In particular, the revised proposals requiring mandatory audit firm rotation after just six years represent a step backwards from the previously announced position.

The proposals do little to address the key systemic risks of the failure of a Big 4 audit firm and the lack of global reach of other audit firms which currently result in a Big 4 auditor being the favoured option for the multinational organizations represented by our members.

Contrary to the statement issued by the European Commission, these proposals will serve to concentrate the market even further as the combination of shorter engagement contracts, a cooling off period and prohibitions on non audit work will preclude participation in the audit tendering process of any firm providing non audit services, who are typically for our membership, other Big 4 firms. Our members face the real prospect of not being able to recommend to shareholders the appointment of precisely those audit firms best equipped to provide a globally robust audit opinion.

Taken together, the reform package will have the effect, both directly and indirectly, of reducing audit quality, particularly during the period of transition, increasing cost and diminishing the value of the audit opinion to investors, without any compensating tangible benefits.

Our survey results emphatically show that the case for reform is overstated. In the view of Hundred Group members, the critical issue to be addressed is not the reform of the audit market, but of regulations governing financial and narrative reporting. The current regime results in audited financial reports which are often too complex, lack meaning and are cluttered with irrelevant, immaterial information which obscures the key financial information being presented."

The full text of the statement issued, together with the Hundred Group's statement of principles on the external audit is available at www.100groupfd.com and is reproduced below.

About the Hundred Group

The Hundred Group represents the Finance Directors of the UK's largest companies. Membership is drawn from the FTSE 100 and other large UK private companies.

Our members collectively employ over 1.8 million people in the UK, and pay, or generate, taxes equivalent to 12% of the UK Exchequer's overall tax take. We seek to assist the development of UK businesses particularly in the areas of tax, reporting, pensions, regulation, capital markets and corporate governance.

Ends

Statement of the Hundred Group of Finance Directors on reform of the external audit market 30 November 2011

As Directors of large public companies, Hundred Group Members recognise the value to shareholders of the financial statement audit. The independent auditor's report is important in ensuring the smooth and efficient operation of capital markets and consequently any action taken to reform this market should be aimed at enhancing, and not diminishing, audit quality.

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Auditor appointment

We strongly believe that the right to appoint, evaluate and determine the tenure of auditors should be retained by shareholders as the strong and necessary arm of corporate governance. In the UK, this is done annually at the Annual General Meeting, such that all auditors only have a tenure of one year. For multinational Companies with subsidiaries in many countries, mandatory rotation every 6 years, particularly combined with a cooling off period, has the effect of reducing competition and choice to an unacceptably low level, especially given current legitimate constraints on appointing, as auditor, a company which is already offering the group consultancy services.

Rotation also risks a reduction in audit quality in the initial and final years of the appointment. We do not recognise, and have seen absolutely no recent evidence of (so called) 'institutional familiarity' and in our view, the regular rotation of audit partners is sufficient to maintain an independent and robust audit. The inevitable reduction in audit quality could only be alleviated by increased audit fees during the transition years – a cost which very few investors have expressed a desire to incur.

Non Audit Services

We agree that it is appropriate to prohibit auditors from undertaking certain specific non audit services (e.g. consultancy) where independence could be impaired. However with appropriate safeguards in place, the quality of both the external audit and other specific non audit services can be enhanced if undertaken by the auditor without any impact on independence, and at lower cost. We also oppose the creation of specialist audit firms as these will undermine the ability of firms to recruit the appropriate quality of audit staff, with consequent highly negative implications on long term audit quality.