

Press release: CMA recommends shake-up of UK audit market

Legislation is needed to address both the vulnerability of the industry to the loss of one of the Big 4, and the current inadequate choice and competition.

The CMA is recommending the separation of audit from consulting services, mandatory 'joint audit' to enable firms outside the Big 4 to develop the capacity needed to review the UK's biggest companies, and the introduction of statutory regulatory powers to increase accountability of companies' audit committees.

The CMA's recommendations follow extensive discussions with audit firms, investors and major UK companies on its [update paper](#) – published in December. They also take account of the recommendations of a major report from the Business Select Committee, and the inquiry into regulation led by Sir John Kingman.

The recommendations are:

Operational split

Auditors should focus exclusively on producing the most challenging and objective audits, rather than being influenced by their much larger consultancy businesses. Given the difficulties with an immediate global structural split, the CMA is – at this stage – recommending an operational split of the Big 4's UK audit work. This will require separate management, accounts and remuneration: a separate CEO and board for the audit arm; separate financial statements for the audit practice; an end to profit-sharing between audit and consultancy, and promotions and bonuses based on the quality of the audits.

More choice to increase resilience: mandatory joint audit

More choice and competition for the audits of big businesses can and should drive up their quality, but the barriers to entry for 'challenger' audit firms are currently large. The CMA recommends mandatory joint audit, to increase the capacity of challengers, to increase choice in the market and thereby drive up audit quality. Challenger firms should work alongside the Big 4 in these joint audits and should be jointly liable for the results. There should be initial limited exceptions to the requirement, based on criteria set by the regulator, focused on the largest and most complex companies. In addition, any company choosing a sole 'challenger' auditor should be exempt. Audits of exempt companies may be subject to rigorous, real-time peer reviews commissioned by and reporting to the regulator. The joint audit requirement should remain in place until the regulator determines that choice and competition have improved enough to address the vulnerability of the market to the loss of one of the Big 4.

Regulation of UK companies' audit committees

It is essential that audit committees choose auditors by seeking those likely to provide the most robust and constructive challenge to the accounting practices of their companies. The CMA recommends that the regulator should hold audit committees more vigorously to account. This may include ensuring that committees report their decisions as they hire and supervise auditors, and that the regulator issues public reprimands to companies whose committees fall short of adequate scrutiny of their auditors.

A 5 year review of progress by the regulator

The regulator should review the effects of these changes periodically, in the first instance five years from full implementation. This should consider in particular: the merits of moving to independent appointment for auditors; whether to go beyond the operational split already proposed; and how to fine-tune the joint audit remedy to adapt to market developments.

CMA Chairman Andrew Tyrie said:

People's livelihoods, savings and pensions all depend on the auditors' job being done to a high standard. But too many fall short – more than a quarter of big company audits are considered sub-standard by the regulator. This cannot be allowed to continue.

The Government now has three reports to hand. In large part, they come to similar conclusions. Conflicts of interest cannot be allowed to persist; nor can the UK afford to rely on only four firms to audit Britain's biggest companies any longer. Early action will require legislation – hence the CMA's proposals.

CMA's Chief Executive, Andrea Coscelli, also commented:

The UK is recognised as having a strong history in the fields of corporate governance and accounting.

Our recommendations, along with improvements to regulation and clarifying the purpose and scope of audits, will ensure the UK strengthens its position.

We look forward to supporting the Government as it considers how best to take forward these changes through legislation, alongside Sir John Kingman's recommendations on regulation and the results from Sir Donald Brydon's review on the quality and effectiveness of audit.

Notes to editors:

1. Market studies are carried out using powers under Part Four of the

Enterprise Act 2002. Market Studies can result in a range of outcomes including recommendations to government, enforcement action and referral for market investigation.

2. The CMA's work has taken account of the Secretary of State's request that it 'be ambitious in its thinking and move swiftly on this issue' ([Letter from the Rt Hon Greg Clark to Lord Tyrie](#), 9 October 2018).
3. The Government has committed to responding to CMA market study recommendations within 90 days. The CMA normally publishes such responses on its website.
4. The Big Four audit firms in the UK are Ernst & Young (EY), Deloitte, KPMG and PricewaterhouseCoopers (PwC).
5. The CMA has taken account of the other reviews of the audit market, including Sir John Kingman's report on the sector regulator, the Government's consultation on his work and Sir Donald Brydon's review of the quality and effectiveness of audit. It has also taken into account the recommendations made by the BEIS Select Committee in its review of the audit market.
6. Media queries should be directed to: press@cma.gov.uk or 020 3738 6460.