SELECTING YOUR AUDITORS

A guide to tendering the external auditor appointment

July 2017
PART 1 - GUIDANCE

1. Introduction

This guide is based on the UK regulatory framework and reflects the tender process to select the auditor of a Public Interest Entity (PIE).

Purpose of the guide

This guide highlights the issues which should be considered by the audit committee as part of an audit tender process. It may form part of the documentary evidence of the work of the audit committee.

Who can use this guide

This guide represents current good practice and can be used as a guide for other organisations and in other jurisdictions. Whilst designed for PIEs, it should also assist other organisations including smaller, listed and unlisted companies and groups and those in the not for profit sectors. Some tailoring of the guidance and questions will be necessary to ensure that they are proportionate for their purposes.

It is focused on the audit committee members but can apply whether or not a formal audit committee exists, in any organisation where the management is separated from the ownership. The term “audit committee” in the following text and questions should be taken to mean “audit committee or other appropriate persons”.

The questions could also be of use to others in the organisation, professional firms with an interest in the audit process and other parties such as institutional shareholders.

The guidance questions have been drawn up in the context of a company. The application of the guidance to group situations will depend on the individual circumstances of the company and the group, the degree to which the audit of the group is undertaken by the parent company auditors and the approach taken by the parent company audit committee in its relationship with the respective auditors of the other group entities.

2. Regulatory requirements

1. The Competition and Market Authority’s (CMA) Order 2014 introduced:

a) Mandatory retendering - FTSE 350 companies must retender their audit at least every ten years (more frequent retendering is encouraged).

b) Measures to strengthen audit committee powers in relation to auditor appointments - only the audit committee is permitted to negotiate and agree audit fees and the scope of audit work, initiate tender processes and make recommendations for appointment of auditors and authorise the external audit firm to carry out non-audit services. The audit committee may also receive submissions from executive management.

The order took effect for financial years commencing on or after 1 January 2015.
2. The EU Audit Regulation and Directive 2014 as incorporated into the Companies Act 2006 via The Statutory Auditors and Third Country Auditors Regulations 2016 introduced:

Mandatory rotation of auditors – PIEs to rotate their external auditors at least every ten years. However, the UK also took advantage of the option to enable the maximum incumbent auditor’s tenure to be extended to 20 years where a retender has taken place.

The legislation took effect for accounting periods commencing on or after 17 June 2016.

A summary of the regulatory requirements are in Appendix 1.

The UK CMA has not mandated a particular form of tender process which companies must follow.

The EU Audit Regulation however, does specify certain criteria which have to be satisfied when a PIE holds an audit tender and these are taken into account in the Companies Act 2006, other applicable legislation (e.g. for PIE insurance undertakings) and in this guidance.

3. Auditor independence

In today’s business climate, boards and audit committees must not lose sight of the need, not only to ensure the independence, objectivity and effectiveness of auditors, but also to be able to demonstrate that they have done so. This is a fundamental requirement when it comes to deciding which firms should be invited to tender.

In order to secure the primary objective of auditor objectivity, there are various provisions relating to independence which auditors are required to follow. However, when considering which firms to invite to tender for the company’s external audit, consideration also has to be given to the independence of those firms that are not in the role of auditor but who currently supply non-audit services to the company. Would such firms be capable of satisfying the necessary independence requirements for the firm to tender, and how do you ensure that they stay independent during the tender period? In the UK, the principal rules on auditor independence can be found in the Financial Reporting Council’s (FRC) Ethical Standard. It should be noted that for some entities the independence requirements will also include those of regulators based in other jurisdictions.

Independence – overarching principle

“In relation to each engagement, the firm, and each covered person, shall ensure (in the case of a covered person, insofar as they are able to do so) that the firm and each covered person is free from conditions and relationships which would make it probable that an objective, reasonable and informed third party would conclude the independence of the firm or any covered person is compromised.”

Source: FRC Ethical Standard 2016

Some audit committees may decide to tender the audit well before the change of auditors is intended to take place, even up to 2 years in advance of the auditor appointment commencing. This approach allows time for the successful firm in the tender process, if not the incumbent, to complete the “cleansing” process and ensure that it will meet all of the necessary independence requirements when it takes up the appointment.

An alternative approach is for companies to consider changing their supplier of certain non-audit services so that the greatest number of firms can be independent at the time of the tender, or for a company to decide to exclude a specific firm from the tender as it does not want to disrupt the provision of another service.

Care is required to ensure that when appointing a new director or member of the senior management team, the appointment does not unduly impact, or be seen to impact upon the independence of the auditors. Reference should be made to section 2 of the FRC’s Ethical Standard. The perceived influence of audit firm alumni on a company’s board also needs to be considered.
4. Company – auditor relationship

A good working relationship between the audit committee, senior management, the finance function, and the auditors is generally a prerequisite for a high-quality audit but should not dilute the level of professional scepticism and challenge that requires to be exercised by auditors.

Monitoring the ongoing relationship between the auditors and the company is essential. This includes the audit committee’s annual assessment of the qualification, expertise, resources, and independence of the external auditors and the effectiveness of the audit process. It should also provide a regular means of determining whether there are areas where the effectiveness or efficiency of the external audit can be improved.

The audit committee is responsible for the awarding and monitoring of non-audit services. Care is required to ensure that legal or ethical requirements relating to non-audit services provided by the audit firm are not breached. This includes the cap on non-audit services. Reference should be made to the FRC’s ‘Guidance on Audit Committees’ and section 5 of the FRC’s Ethical Standard.

The audit committee is responsible for developing a policy on the provision of non-audit services which should be approved by the board. This policy should include those services which can be carried out by the auditor and the approval limits. Normally this includes a level for management to sign off at (fairly low), a level requiring audit committee chair sign off and finally a level which requires full audit committee approval.

5. Why tender?

There may be regulatory requirements or other business reasons for tendering. Regardless, there is a need to establish clear objectives of what the company is looking to achieve from the process, beyond just compliance with legislation.

The audit committee should keep shareholders informed through the Audit Committee Report as to when the company plans to tender and keep them updated when the formal tender is commenced so that they have the opportunity to engage with the company if they desire.

Other reasons for tendering might include:

(a) a significant change in the scale, or geographical reach of the group;
(b) changes of key personnel in the company or audit firm;
(c) an unsatisfactory review of the incumbent auditors’ performance;
(d) the desire to test the market to make sure the service being offered is the best for the company; or
(e) helping to facilitate a review of the value for money of the current service offering, subject to audit quality not being compromised.

Once established, it is helpful to ensure that the objectives are included in the Request for Proposal (RFP) which is subsequently issued.

6. When to tender?

The tendering of an audit should be on the audit committee’s forward agenda - appropriate planning is critical for the success of the process.

With the introduction of mandatory tendering and mandatory rotation for the auditors of PIEs, the regulatory framework surrounding auditor appointment has changed significantly. Audit committees now need to give greater consideration than before to the appropriate timing of a tender process. Ultimately, the CMA Order and Companies Act 2006 requirements (see Appendix 1) establish statutory deadlines by which companies will need to retender their audit/rotate their auditors. The audit committee needs to ascertain these deadlines. Companies may tender their audit at any time and decide to do so for reasons other than statutory requirements (as noted above).

Consideration also needs to be given to the other entities within the group and the legislative and other requirements that they need to comply with, whether such entities are within the EU or elsewhere. The UK is one of the few countries to have taken advantage of the option within the EU Audit Regulation to allow an auditor to be in office for a period of up to 20 years (subject to the auditor being reappointed following a retender(s) at least every ten years). A co-ordinated approach is needed to ensure that audit committees appropriately involve the audit committees of any related PIEs in the process.

Changes in key personnel such as the CFO, Audit Committee Chair or Audit Engagement Partner may present a trigger for an audit tender (for example, where it impacts on independence). Any such changes (recent or planned) might impact on the timing of the decision. Other possible triggers might relate to known or expected operational or strategic changes to the business. This will include situations where significant acquisitions or disposals are envisaged. Planned significant changes to an entity’s IT system may also provide such a trigger.
Even if the audit committee does not wish to put the audit out to tender until the latest possible deadline, it should still ensure that it establishes an appropriate process as it may have to tender earlier than it anticipated e.g. if the annual review of the performance of the external auditor does not meet expectations. Also, there may be a benefit of having a slightly early tender to allow the firm awarded the audit to shadow the incumbent auditor through the year end for example, in a very controlled process.

Companies could consider disclosing their audit retendering policy in the audit committee report in the annual report but, at a minimum, should indicate when they intend to next tender the audit by disclosing their intention to tender a year or more ahead of the process.

There are certain disclosure requirements in situations where the company has not tendered the audit in the past five years (as detailed in the CMA Order). A summary of this and current legal requirements relating to audit tenders and audit firm rotation is at Appendix 1.

7. Establishing key assessment criteria

Prior to undertaking the tender process the audit committee has to identify the key criteria which it will use to assess the bids that it will receive from the prospective firms. In a scenario when the maximum period of audit tenure has not been reached, the list of prospective firms may include the incumbent auditor, although where the incumbent only has a few years until it has to rotate off, consideration needs to be given as to whether this is appropriate.

It is important to establish key assessment criteria just after setting the objectives for the tender process. Tender documents should be transparent and state the non-discriminatory selection criteria which will be used to evaluate proposals.

The audit committee has to take on board that the objective of the audit is to provide the shareholders of the company with assurance that the company’s financial statements can be relied upon.

At the heart of the assessment criteria must be “audit quality”. The overriding objective of undertaking an audit tender should be to seek to ensure that the company has the best possible auditor for the company’s needs.

There is no agreed definition of audit quality however in practice it is accepted that there are various attributes which help to ensure that a quality audit is performed. Such attributes are to be found in the Financial Reporting Council’s ‘Audit Quality Framework’ (2008) which recognises the following key drivers of audit quality:

(i) The culture within an audit firm;
(ii) The skills and personal qualities of audit partners and staff;
(iii) The effectiveness of the audit process;
(iv) The reliability and usefulness of audit reporting; and
(v) Factors outside the control of auditors affecting audit quality.

Examining each of the above drivers which are within the auditor’s control:

(i) The culture within an audit firm

Information on each of the potential candidate firms may be obtained from their respective Audit Firm Transparency reports. These reports set out how the respective firms have complied with the requirements of the UK Audit Firm Corporate Governance Code and highlight how they seek to ensure audit quality.

The initial request for information from the firms invited to tender may also ask for the firms to explain how they ensure they comply with applicable independence requirements as well as their approach to ensuring an appropriate ethical culture within the firm.

(ii) The skills and personal qualities of audit partners and staff

Assessment needs to ensure that the person responsible for the signing of the audit report and their supporting engagement team (once confirmed) have the necessary attributes and skills. The initial screening process should assist in ensuring that the firms put forward the most suitable audit engagement partner candidates (see 1.7 below).

(iii) The effectiveness of the audit process

Whilst only the incumbent firm can be assessed directly, members of the Board or audit committee may have knowledge of other audit firms through other services they provide to the company or professional networks and other directorship appointments that they may hold.

The firms should be asked to explain the audit approach that they will adopt and illustrate how they believe this best meets the needs of the organisation. Firms other than the incumbent will need to be provided with detailed information about the organisation to help them identify what they believe to be the key business and audit risks (see “data room” below). The audit approach proposed should display a clear understanding of the company’s business, its industry sector, the major risks identified and how the auditor will respond to those risks.
The auditor’s response to the identified risks would be expected to include an assessment of materiality, how specific high-risk areas would be audited, the approach and scope of audits of other undertakings within the group and the balance of compliance and substantive testing. The audit firm may also be asked to explain its approach to innovation including the use of specific audit tools such as data analytics.

The use of certain scenarios to allow the auditors to illustrate their professional judgement may be helpful. This might involve asking the prospective candidates to comment on the company’s accounting policies. Additionally, as communications from the auditor are deemed to be a key part of audit quality, auditors should be asked to explain their approach to communicating with the audit committee.

**External Inspection Reports**

Reference can be made to the audit inspection reports issued by the Audit Quality Review Team of the FRC. These are published on an annual basis for most of the larger firms and grade the audits reviewed into the following categories:

- Good (category 1);
- Limited improvements required (category 2A);
- Acceptable overall with improvements required (category 2B); and
- Significant improvements required (category 3).

Depending on the jurisdictions in which an entity operates, public inspection reports may also be available in other countries.

**Expertise in the specific business sector**

The audit committee has to ensure that it appoints an auditor that has the necessary knowledge and skills to audit the business in question. Care is needed to ensure that the firms selected all possess the necessary skills and expertise to perform a quality audit.

**Geographical coverage**

The extent to which geographical coverage is required needs to be considered. This needs to be based on the perceived strength of a firm’s network in the relevant jurisdictions in which a company operates.

(iv) The reliability and usefulness of audit reporting

The auditor is required to report on the key audit matters they encountered during the audit⁶. The respective firms could be asked to explain the approach that they have adopted to this change in reporting and to provide copies of example reports to illustrate this.

The FRC’s publication *Audit Quality – Practice Aid for Audit Committees* also provides some useful pointers for assessing audit quality.

**Key criteria**

Having considered the above it is likely that the key criteria will encompass at least some of the following:

- The firm and audit team’s knowledge and experience and expertise of the relevant industry sector(s);
- The lead partner and firm’s audit quality record;
- The respective firms’ geographical coverage in relation to group entities; and
- The extent to which technology will be integrated into the audit approach.

**8. The tender process**

Audit tenders are costly exercises for both management and the audit firms. Therefore, it is essential that they are planned, and executed on a professional basis in order to minimise the time spent by all parties. Different tender processes can be adopted but ultimately the responsibility rests with the audit committee. There is a need to ensure that all members of the audit committee are engaged on this issue and not just the Audit Committee Chair. The audit committee (or sub-committee) may utilise the assistance of entity staff or engage the services of an external firm of consultants to assist in the process. However, overall control and the ultimate decision must remain solely with the audit committee.

Whilst in theory an audit tender can be conducted at any time, there are certain practicalities that need to be considered. The aim should be to conduct the tender at the time at which it will have least impact or disruption on the business concerned.

Good practice tendering usually follows four stages (see over).
Establish a project committee

Once the audit committee has decided that the audit is to be put out to tender, the audit committee should ensure that someone is given responsibility for managing the project i.e. ensuring that the project is progressing as per the timetable. This might be the Audit Committee Chair or Group Financial Controller.

Whilst the audit committee must retain control of the process it may elect to delegate at least some of the work to a sub-committee to oversee the logistics of the tender process. This sub-committee would normally include the Audit Committee Chair, CFO and project manager.

For multi-national companies, consideration will need to be given to the extent to which the tender process will be centralised or if overseas management will be involved in the process.

Determine the timetable

Key matters to be included in a timetable are:

- Key project dates;
- What information will be made available to candidates via a data room;
- What access will they have to management; and
- What access will, they have to the incumbent auditor.

It is important to set the dates early. The Request for Proposal (RFP) should set out:

- When the tender will take place;
- The dates when the data room will be open; and
- When the management meetings will take place.

Determine the list of firms to be invited to tender

Speaking directly to various firms at the pre-tender stage can help establish whether they have the capability to conduct the audit before being included in the tender process. Preparation work can also include:

- Reviewing Transparency Reports (published by the firms);
- Reviewing Audit Inspection Reports (published by the FRC);
- Requesting specific capability documents (from the firms);
- Issuing targeted/relevant questionnaires (to help gather information from the firms directly).

Having determined the purpose of the tender process and the possible candidates, the audit committee may decide to shortlist the number of audit firms invited. Firms should be requested to review their independence (see section 1.2) and identify any matters which would need to be addressed if they were to be appointed as auditor.

Required skill-set – audit engagement partner

The level of skills and experience required in the audit engagement partner will need to be clarified. To facilitate identification of the most suitable candidates, consideration should be given at this stage to inviting each firm to select up to three partners for the audit committee to determine who would be best to lead the respective firms’ proposals. This can be viewed as a pre-screening phase where meetings are held with the prospective partners. This also allows a discussion of the respective firms’ capabilities and any independence issues etc. To ensure continuity, it is worth requesting a commitment from the audit firm that the selected partner, if chosen, would be available for a five-year period.
Evaluation

Audit committees need to decide on a means of evaluating the prospective candidates. Audit committees are increasingly using a scorecard to assess the firms’ offerings. This should be applied across the entire tendering process to ensure that the key information is taken into account, including management views following their meetings with the audit firms. This is important as the audit committee has to ensure that there is careful evidencing of the tender process up to and including the rationale behind its first and second choices of auditor.

A decision also has to be made on the most appropriate means of making the final decision (vote or consensus) and when this should be taken (immediately following the presentations, or a few days later).

Request for proposal (RFP)

All potential bidders should be treated fairly to ensure a fair competitive process. The RFP should be sent to all the prospective firms and seek to ensure a level playing field. This would normally be sent to the Head of Audit at the respective firms. The firms in questions should be asked to sign a confidentiality agreement prior to being provided with information about the entity.

The content of the RFP should cover the main aspects of the tender process including:

- the timetable for the process (including key dates such as the deadline for submissions);
- key contact details;
- the deliverables that will be expected from the audit firms; and
- the criteria that will used to make the final assessment.

If the incumbent is not tendering, they may be a useful source of advice. They will have seen tenders from the other side of the table and so have a good idea of what works and what does not in terms of process and in terms of what firms find useful in the data room when they are trying to better understand the business.

Communicating assessment criteria will help to ensure that each of the prospective firms has sufficient information to formulate their suggested audit approach and hence submit an informed tender. The format of the RFP should be ‘clear and concise’. Limits on the length of the tenders to be submitted are often set e.g. twenty pages with ten pages of appendices.

Data room

Creating a secure online data room can prove effective. It makes it easier for tender participants to access relevant information on the company, at a time which suits them.

Access to the data room needs to be properly controlled and the main contact person for questions confirmed.

The information to be contained in the data room is a decision for the audit committee but would normally include the following (not exhaustive and more detail is included in the guidance questions below):

- Details of the entity i.e. group structure including geographic locations, business type and organisation charts;
- Accounting information including statutory accounts, group reporting requirements;
- Relevant audit committee and board papers; and
- The incumbent auditor’s most recent audit plan and audit scope (authorisation required from the incumbent).

Participants should not be overburdened with too much information as this could hamper their knowledge building efforts.

Meet management

The firms should be given the opportunity to meet with key personnel to allow them to gain a more comprehensive understanding of the entity and its business model, risks and internal controls. It also helps to strengthen the quality of submissions and tailor the service on offer. Meetings with local management at key sites may be required.

It is essential that the level of access should be the same for all firms tendering (including the incumbent if applicable).

To help manage the process efficiently, consideration should be given to informing the firms that access is limited to specific dates and locations to minimise ad hoc requests.

References

The need to obtain references for the audit firms can be considered.
Submission

The firms submit their respective proposals in response to the RFP by the due date.

Depending on the number of firms being asked to tender, they might all be asked to present their proposals to the sub-committee or audit committee at this stage. This provides an opportunity to shortlist the number of firms who will compete at stage 3. If this approach is adopted then the successful firms would normally be provided with the opportunity to refine their written proposals prior to giving their final presentations at stage 3. Of course, the strength of the written submissions alone may be used as the basis for selecting the firms who make it to the third stage.

Stage 3 Presentations

- Format and focus of presentations of service offerings
- Selecting attendees from the audit firms
- Fees

Selecting attendees from the audit firms

Identifying the key audit personnel to be invited to the presentation to help inform an assessment needs careful consideration team. For example, the audit partner, director and manager. The involvement of audit partners responsible for overseas operations, IT, other specialists and more junior members of the team might provide a broader view. However, too many people can become cumbersome.

Fees

The audit committee should be responsible for the audit fee negotiations.

Whilst an assessment has to be made in relation to the fees which are being proposed by the prospective candidates, audit quality must be the overriding factor in the decision-making process. The key factor is to choose an auditor who meets the tender objectives, quality standard and organisation's needs.

The audit committee should decide whether the fee should be negotiated before or after the decision is made on which firm to appoint. Some prefer to identify the preferred auditor without considering the fee at this stage (for example, using separate envelopes for the fees) so members can evaluate and rank the offerings based on quality first. Fee negotiations would follow.

Stage 4 Decision

- Recommendation to the Board
- Announcement
- Feedback to bidders

Recommendation to the board

The audit committee makes its decision and submits its recommendation to the Board with a paper supporting its rationale. The audit committee’s recommendation must contain a minimum of two choices with a duly justified preference for one candidate. In its recommendation, the audit committee shall state that its recommendation is free from influence by a third party and that no clause restricting its options has been entered into by the company.
Announcement

The Board will decide which audit firm should be appointed and then announce the decision. The Board then must present its proposal to the shareholders at the next Annual General Meeting, including the audit committee’s recommendation to the Board, for their decision. If this proposal to shareholders departs from the preference of the audit committee, the proposal shall justify the reasons for not following the recommendation of the audit committee. Additionally, in such circumstances the firm being proposed by the Board must have participated in the selection procedure.

Feedback to bidders

It is helpful if feedback is provided to the bidding firms on their performance during the tender process with reasons why the successful firm was chosen.
PART 2 - AUDIT TENDER GUIDANCE QUESTIONS

Pre-tender

1. Has the audit committee formulated a policy for how often it intends to put the company’s external audit out to tender and if so, has that policy been agreed at board level? As a minimum has the audit committee established when it has to tender the audit given the statutory deadlines?

2. Is the company’s tender process likely to be impacted by requirements in other jurisdictions in which the company has a presence e.g. EU member states?

3. Have the reasons for putting the audit out to tender been clearly debated so the committee can discuss why it intends to do so with the board, and if appropriate major shareholders and other parties, such as regulators in regulated industries, prior to starting the process? Clear objectives should be established at the outset.

Note: The reason for initiating the tender may be that the company is required to do so.

4. Has consideration been given to seeking views from other appropriate parties independent of the Board on what possible firms to include in the process?

5. The decision-making panel for selecting the auditor of a PIE must be the audit committee assisted as appropriate by a sub selection committee. If the entity is not a PIE has the decision-making panel been chosen?

6. Has the most appropriate time in the year to undertake the tender process been confirmed?

7. Has consideration been given to holding the audit tender well in advance of the planned appointment date? This may be necessary to ensure that possible candidates for appointment have sufficient time to “cleanse” themselves from any prohibited non-audit services that they are currently providing, or to provide time for the incoming auditor to shadow the incumbent say through a year-end process.

Tender Process Stage 1 – Preparatory work

8. Have board members identified any independence issues that they may have with any of the firms being considered?

9. Has a project committee been established to oversee the tender process?

10. Has an appropriate individual been given responsibility for leading the tender process?

11. Has a timetable been prepared for the process, including providing adequate access for the firms to senior management, finance personnel as well as the audit committee? Is the timetable feasible given the likely demands on the time of senior personnel?

12. Has an analysis been performed to ascertain what audit firms it would be appropriate to invite to participate in the tender process?
13. Does this analysis include:

a) Reputations of audit firms?

b) Industry knowledge and expertise?

c) Any past experience of audit firms?

d) Financial stability, risk profile and litigation record?

e) Any personal references?

f) Nature and reach of auditor’s network?

g) A review of the Audit Firm’s transparency report

h) A review of the Inspection Report published on the firm by the FRC’s Audit Quality Review Team, if applicable. (This may also include consideration of reports by overseas inspectors).

14. Have preliminary meetings been held with prospective firms to seek to get an understanding as to whether that firm has the capability to conduct the audit?

15. Has consideration been given to the skill set and experience being looked for in the audit engagement partner and have each of the firms been invited to select a small selection of possible candidates for initial discussions?

16. Have the key assessment criteria (scorecard) been established on which the ultimate decision will be based and should also be used to score each firm’s written submission and presentation? Does this include reference to the FRC’s key drivers of audit quality? This will include a list of necessary skills and services (subject to independence requirements) required of the auditors.

17. Do any potential conflicts exist, such as existing relationships (including with industry competitors to your business), engagements with the company or regulatory or professional requirements, which could exclude a particular audit firm from the tender process? If any such conflicts currently exist will these still be an issue at the date the audit appointment is due to commence? Has the company started to manage the work being awarded to those firms invited to tender so as not to create any independence issues.

18. Do you already use any of the firms selected to provide non-audit services? Their performance may provide an indication as to the suitability of the firm concerned.

19. Does the company’s audit or other assurance requirement necessitate specialist skills – e.g. actuarial skills, and does each of the identified potential candidates possess these skills?

20. Do the audit firms identified have the necessary expertise of the sector(s) in which your company or group operates?
Tender process – Stage 2 – Audit proposals

21. Has the audit committee prepared a ‘Request for Proposal’ (RFP) document which will allow all parties to tender on an equal footing? The scope of the work being tendered needs to be clearly defined in the tender document. It should clearly set out the details of the tender process including the evaluation criteria to be used and the key contact at the entity and relevant dates.

22. Have detailed specifications been prepared as to the desired content of the written proposals to be submitted by the firms and the maximum length?

23. Does the RFP explain the process by which those tendering would get access to the following company information:

   a) A schematic of the group’s structure, including geographical locations and legal status of entities?

   b) Financial performance?

   c) Control framework?

   d) IT infrastructure and strategy?

   e) Internal audit structure, role and responsibilities?

   f) Risk management processes?

   g) Previous audit committee minutes?

   h) Previous audit committee papers?

   i) Organisation structure charts?

   j) Prior year accounts and other corporate information as deemed appropriate?

   k) Accounting procedures manuals?

   l) Reporting procedures manuals?

   m) The incumbent auditor’s audit plan and scope for the most recent audit (Authorisation from the firm will be required)?

   n) Other relevant information?

      (access to all of the above information will probably be via an online secure data room)
24. Have the relevant audit firms signed a confidentiality letter prior to receiving information?

25. Have the relevant audit firms provided a statement of independence and have they got policies in place to ensure they remain independent until the tender process is completed?

26. Where time and cost constraints permit, have plans been made for the shortlisted firms to visit selected typical company or group operations or to “meet” overseas management (possibly via video conference)?

27. Has a process been established for the management of any visited operations, or those meeting the participants to score the shortlisted firms?

28. Following submission of their written responses will each of the firms be asked to present their proposals at this stage to seek to reduce the field before stage 3? The submissions and presentations should be assessed based on the key assessment criteria.

**Tender process – Stage 3 – Presentations**

29. Has a list of questions been prepared to be addressed in the final presentations? Has the required length of the presentation document been limited in size included appendices?

30. Has it been decided what personnel from the shortlisted audit firms should be invited to attend?

31. Will the shortlisted auditors be asked to comment on the group’s accounting and financial reporting manuals, consolidation pack, and other relevant documentation used by all company or group operations?

32. Will the firms be set a technical challenge – if so, has this been prepared?

33. Consider, who from the company other than audit committee members should be invited to attend the face to face presentations - and have dates been reserved for these (CFO and the Financial Controller would normally be in attendance)?

34. Has it been ensured that the firms’ submissions and presentations will be assessed based on the key assessment criteria?

35. Are the people presenting to the audit committee those that will conduct the audit?

36. Are expected audit hours and scale rates comparable with other firms?

**Tender process – Phase 4 – The decision**

37. Has a draft press communication been prepared and agreed in advance with the shortlisted parties on a confidential basis, together with the intended timing of its release after the final selection process has been completed?
38. Have the following factors, in no particular order, been considered in making the final decision on the appointment of the auditors:

a) Reputation and financial stability of the firms?  

b) Audit approach?  

c) Views of shareholders, regulators and financiers if felt appropriate?  

d) Previous experience and recommendations from others?  

e) Value for money?  

f) Reputation, personality, perceived quality, experience, enthusiasm, demonstrable interest in the company, of the key audit partners and staff?  

g) Depth of audit team expertise and technical back-up, including access to any necessary specialists?  

h) Business understanding?  

i) Industry expertise?  

j) Geographic service capability?  

k) Independence and objectivity?  

l) Procedure for ensuring continuing independence and objectivity?  

m) The extent technology will be integrated into the audit approach?  

39. Has the audit committee properly documented its conclusions?
40. Has the audit committee conveyed its decision to the Board in the prescribed format?

41. Has the Board made its decision and then announced it?

42. Has the Board then presented its proposal to the shareholders at the next AGM (including the audit committee’s recommendation)? If this is different from the audit committee’s proposal then the reasons shall be justified.

Points to note

If the decision is made following a tender process to change the current auditor and appoint new auditors, then there will be various legal and procedural matters which will need to be addressed. For companies which do not have in-house legal departments, this may involve seeking external advice. This should be undertaken once a decision has been made but prior to any public announcement.
ENDNOTES

1. PIE includes entities incorporated in an EU member state with securities listed on a regulated market, credit institutions and insurers.

   The definition of PIEs for the purpose of the Audit Regulation is set out in The Statutory Auditors and Third Country Auditors Regulations 2016 (no. 649).

   ‘Public interest entities’ means:

   a) an issuer whose transferable securities are admitted to trading on a regulated market;

   b) a credit institution within the meaning given by Article 4(1)(1) of Regulation (EU) No. 575/2013 of the European Parliament and of the Council (f), other than one listed in Article 2 of Directive 2013/36/EU of the European Parliament and of the Council on access to the activity of credit institutions and investment firms (g); or


2. On very rare occasions and subject to FRC approval, 22 years may be possible.

3. FRC Ethical Standard [www.frc.org.uk](http://www.frc.org.uk)


5. On very rare occasions and subject to FRC approval, 22 years may be possible.

APPENDIX 1 - AUDIT TENDERING AND ROTATION: SUMMARY OF REGULATORY REQUIREMENTS

(i) Competition and Markets Authority (CMA) order

The CMA Order came into force on 1 January 2015 and applies to Financial Years beginning on or after 1 January 2015. The provisions of this Order apply to a Company from the date on which it enters the FTSE 100 or FTSE 250 index until the date on which it ceases to be a FTSE 350 Company.

The CMA requires the audits of FTSE 350 companies to be retendered not less frequently than every ten years. If a FTSE 350 Company has not held a tender in relation to five consecutive years then the audit committee must set out in the audit committee report relating to the fifth Financial Year in relation to which there has been no Competitive Tender Process:

(a) the Financial Year in which the FTSE 350 Company proposes that it will next complete a Competitive Tender Process; and
(b) the reasons as to why completing a Competitive Tender Process in the Financial Year proposed are in the best interests of the FTSE 350 Company’s members.

The requirement for this information applies to each subsequent year until the company has completed a tender.

The CMA’s Order also introduced measures designed to strengthen the accountability of the auditor to the audit committee. These include a stipulation that only the audit committee is:

• permitted to negotiate and agree audit fees and the scope of audit work;
• influence the appointment of an audit engagement partner;
• initiate and supervise competitive tender processes; and
• make recommendations for appointment of auditors and authorise the auditors to carry out non-audit services.

Transitional provisions

The CMA has aligned its transitional provisions with those of the EU Audit Regulation that applies to Public Interest Entities (see below).

See also the Explanatory Note Order 2014 - The Statutory Audit Services for Large Companies Market

(ii) EU Audit Legislation

These requirements require a Public Interest Entity (PIE) to rotate its auditors every ten years unless a public tender is held at the end of year ten. If the incumbent auditor is successful then the period may be increased to twenty years. These requirements have been enacted into the Companies Act 2006 via ‘The Statutory Auditors and Third Country Auditors Regulations 2016’. In the UK a PIE may retender before year ten and this will allow the incumbent audit firm, if reappointed, to serve for another ten years. In total, the audit firm’s tenure must not exceed 20 years, unless on a very rare occasion where FRC approval is sought to allow the incumbent audit firm to serve for another two years.

(1) In the case of an auditor who was first appointed in respect of a financial year beginning before 17th June 1994 and who continues to hold office on 17th June 2016, “the maximum engagement period” means the period ending on the day before the first day of the first financial year of the company that begins on or after 17th June 2020.

E.g. the audit firm was appointed in 1992 and the company’s year-end is 31 December. The audit firm’s last year of engagement would be the year ending 31 December 2020.
(2) In the case of an auditor who was first appointed in respect of a financial year beginning on or after 17th June 1994 and before 17th June 2003 and who continues to hold office on 17th June 2016, “the maximum engagement period” means the period ending on the day before the first day of the first financial year of the company that begins on or after 17th June 2023.

  e.g. the audit firm was appointed in 1997 and the company’s year-end is 31 December. The audit firm’s last year of engagement would the year ending 31 December 2023.

(3) In the case of an auditor who was first appointed in respect of a financial year beginning on or after 17th June 2003 and before 17th June 2016 and who continues to hold office on 17th June 2016, “the maximum engagement period” means whichever of the following periods is longest:

(a) the period ending on whichever is the later of:

  (i) the day before the first day of the first financial year of the company that begins on or after 17th June 2016; or

  (ii) the last day of the period of ten years beginning with the first day of the first financial year of the company in respect of which the auditor was appointed,

  e.g. the audit firm was appointed in 2005 and the company’s year-end is 31 December. The audit firm’s last year of engagement would be the year ending 31 December 2016. However, in this scenario the audit firm could be reappointed if it was successful in a tender process.

The Department of Business, Energy & Industrial Strategy (BEIS) has sought to clarify that: the first subparagraph of Article 17(8) of the EU Regulation makes clear that for the purposes of that Article “the audit engagement should be calculated as from the first financial year covered in the audit engagement letter”. BEIS (and the European Commission) consider this should be understood also to apply to the calculation of the duration (both the beginning and end) of the audit engagement for the purpose of transitional provisions e.g. the audit engagement in relation to the calendar accounting years beginning on 1 January 2000 and ending on 31 December 2023 should be understood to have begun and ended on those dates even though, after the end of the final year, the auditor will have to continue to work to complete the audit of the accounts for that year.
APPENDIX 2 - ACKNOWLEDGEMENTS

The ICAS Policy Leadership Board would like to thank the following members for assisting in the preparation of this guidance:

ICAS Business Policy Panel

Alan Ferguson
Non-executive director at Johnson Matthey plc, Croda International plc, the Weir Group plc and Marshall Motors Holdings

Ross Paterson
Finance Director, Stagecoach Group plc

ICAS Council

Andrew Dougal
Non-executive director of Carillion Plc and Victrex plc

It should be noted that the above members were acting in their personal capacity and were not representing the organisations for which they work.

The guidance was drafted by:

ICAS Staff

James E Barbour
Director, Policy Leadership
ICAS

Alice Telfer
Head, Business Policy & Public Sector
ICAS