Why Grant Thornton and BDO want audit reform

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The two issues at the centre of this debate are concerns over the limited range of choice and competition in the market, as well as conflicts of interest, both real and perceived. Together, Deloitte, EY, KPMG and PwC serve 97% of the most lucrative contracts on the market.

The concern is that the Big 4 have an unfair advantage in the auditing market when it comes to the biggest contracts, which may affect audit quality. This is why the UK's fifth biggest firm, Grant Thornton, on September 11 called for an independent public body to be set up to oversee the tendering for public interest entities (PIEs) such as that FTSE 350 companies.

"Going back to earlier in the year, our firm decided to withdraw its bids for FTSE 350 contracts because we were coming a heroic second to the Big 4," Jon Roberts, head of audit at Grant Thornton, told *International Tax Review*.

"It was a big decision for us, but it was a matter of principle," he stressed. "Until there is an equal playing field, we shouldn't be playing such a role in an unfair game."

Grant Thornton suggests an independent body could help to resolve the imbalance in market share for auditing work.

"We would take the decision away from the companies and give it to an independent public body. It could take the form of shareholder representatives and representatives of other stakeholders as well," Roberts said. "There are precedents for this in English local authorities. There are some very complex authorities, and more than 90% of their auditors are appointed by an independent body."

The sixth-biggest firm, BDO, would rather see a 60% market share cap imposed on the Big 4. This would mean the biggest accounting firms would have to turn down 40% of their FTSE 350 audit contracts and allow other firms to take up those clients.

Gervase MacGregor, head of advisory services at BDO, explained that the proposal would need to be clear on the composition of the public body and its exact purpose. In theory, such a body could choose the auditors for a company, whereas it used to be up to the board of directors.

"Having a public body policing auditor selection may deliver change, but it would be deeply unpopular," MacGregor said. "You'll effectively be taking away the power from shareholders and companies to pick their own auditors. A lot of the companies on the buy-side [will] object to this quite strongly."

Although Grant Thornton does not share the same enthusiasm for a cap, it believes an independent public body could manage this too.

"We're not in favour of a market share cap alone to address the high levels of concentration in the Big 4," Roberts said, but he stressed that to address this market dominance of the Big 4 impartially, market management with an independent body is necessary. He added that the firm's proposed independent auditor arrangement could also facilitate caps on market share.

Another version of BDO's proposal would cap the audits of PIEs. So the Big 4 would only be allowed to audit 300 PIEs each, totalling 1,200 PIEs across the four firms. The other PIEs would be opened up to the competition. MacGregor argued that this would improve quality on both sides.

"Firms would be encouraged to choose clients on quality and not exclusively on price," MacGregor said. "If you speak to clients, they don't want the cheapest audit if it doesn't offer quality."

Separating tax and audit

The British accounting industry has faced difficult questions over regulatory standards since the Carillion scandal. However, the debate is not confined to the UK – it's global. The questions facing British auditors are the same as those being raised around the world.

Wim Wuyts, CEO of WTS Global, says keeping tax advice separate from auditing work is a crucial part of his firm's strategy.

"We all have a responsibility to manage and avoid conflicts of interest, from the board of directors through to the audit and finance committee, through the CFO, through the service itself," Wuyts told *ITR*.

"As a global tax service provider, we take it from a strategic point of view," he continued. "We want zero potential for conflicts of interest when it comes to serving the client. We want to create the strongest tax-only alternative when it comes to compliance and advisory work."

This is why some observers believe the auditing sector has to separated from tax advice, but opponents argue that this would undermine the level of service.

One tax director at a major fintech company told *ITR* that the separation of tax services from auditing might not change much for their business because they already use different firms for each area. This is due to the existing constraints on auditors.

"The problem will be how accounting firms audit tax, as they will not necessarily have the expertise, which will mean the audit cost for tax work will inevitably increase and the process will become really inefficient," the tax director said.

"This would not change the independence of the firms, but there would be a question of how the accounting firms would retain tax knowledge as they lose their tax teams," they added.

If regulations are like cobwebs, only the smaller firms will get caught. The most established firms will likely continue to have the upper hand over medium-tier firms or newcomers even if new restrictions are introduced.

"It's a bit like the banking crisis of 2008," Wuyts said. "As long as there are no major disasters, the authorities will not intervene until it's too late."

"We should not be waiting for that incident that will attract the media's attention and push the investor community and the firms to make the necessary changes," he added.

WTS is not alone in taking a tax-only strategy. Taxand and Andersen Tax are trying to establish themselves as global players in a similar way, albeit covering different sections of the same market.

It might not be a coincidence that these firms were launched at roughly the same time. If the tax world is forced to move further away from auditing, tax-only firms may be well positioned for the new era.