

COMMENTS OF THE
INSTITUTE OF CREDIT MANAGEMENT
ON THE FINANCIAL REPORTING COUNCIL DISCUSSION PAPER:
CHOICE IN THE UK AUDIT MARKET

The Institute of Credit Management is the largest professional credit management organisation in Europe. Its 8,500 members hold important, credit-related appointments throughout industry and commerce, and we welcome the opportunity to comment on this paper.

General Observations

Members of the Institute consider that effectively having only four audit firms to serve large business in the UK is too restrictive. We understand that market forces will always restrict the number of firms capable of large or complex audits, however, it would be better if there were a choice between at least six or seven firms, as was the case in the late 1980s.

One concern that was raised by Institute members, is the conflicting interests and lack of independence that prevails between the four firms and big business, especially as a result of the supply of highly remunerative non-audit financial services by the subject firms.

Question 1: Do you agree that the focus of the debate should be on the degree of choice in the market for audit services to large public companies, rather than other features of this market?

The Institute agrees. Regardless of the fact that price remains a relatively unimportant factor in auditor selection, the small number of candidates reduces the opportunity for competitive pricing.

Question 2: What do you regard as the most important criteria for evaluating any opportunities for mitigating risks arising from the level of choice in the audit market.

In the Institute's view, adherence to Sarbanes-Oxley rules should reduce the risk to confidence in corporate governance, but perhaps further consolidation should be encouraged and facilitated outside of the Big Four firms.

Question 3: We invite views on how different groups, acting individually or collectively, could increase the propensity of non-Big four or new firms to seek to be major players in the market for audits of large companies.

It is the view of the Institute that the current Big Four, have attained their position through a natural process of growth, and then consolidation. The Government could do more, and facilitate that evolutionary process, by giving tax incentives, and changing the legislative framework to replicate that development among the smaller firms.

Question 4: We invite views on how the propensity of companies and their audit committees to purchase audit services from non-Big Four firms could be increased.

Members of the Institute made two suggestions, namely:

- (i) to publish, on a well publicised Government website, a database showing eligible firms and the areas that they specialise in, with links to other specialist websites.
- (ii) statutory amendments to discourage the Big Four from taking any measures that would obviate restrictive practices that may impede a change-over to other auditing firms.

Question 5:

In the Institute's view, such is the strength of the Big Four that increased choice will not come naturally in the short-term. Members of the Institute consider that Government needs to take a lead in driving change. A combination of changes to existing laws and regulations and other steps to encourage a shift in attitude will be required.

Question 6: We invite views on steps that could be taken to mitigate the risk of unnecessary withdrawal of a firm from the market.

The Institute considers that there is always a risk that an auditing firm may unnecessarily withdraw from the market as a result of, for example, a financial scandal, damaging litigation or other factors. Transparency should be enforced and assured. All auditing firms must have adequate insurance cover against catastrophe, and the rules preventing a conflict of interest should be rigorously enforced and continuously reviewed.

Question 7: We invite views on steps that could be taken to mitigate the effects of a voluntary or involuntary withdrawal of a firm from the audit market.

Members of the Institute commented that this question approaches the symptoms of the problem rather than the causes. However, a number of contingency measures need to be in place to ensure that the impact on companies and the economy is minimal.