

Professional Services

Rules focus on audit clean-up

Mark Fenton-Jones

The European Commission is pushing for tough rules that would force large firms to abandon their consultancy businesses and share audit work with smaller rivals.

According to reports, European Union internal market commissioner Michel Barnier will officially reveal to the profession in November that he wants companies with balance sheets greater than €1 billion (\$1.4 billion) to hire two auditors to conduct a joint audit of their books, including at least one firm outside the big four of PwC, KPMG, Ernst & Young, and Deloitte.

Under the proposed rules, auditors would also be prevented from working for the one company for more than nine years, which the EU hopes will bolster independence and stimulate competition.

The EU also wants to stop auditors undertaking non-audit work for the same client because of the potential conflict of interest.

This rule change recalls the fallout from the collapse of United States energy company Enron in 2001 and the end of Arthur Andersen, then one of the five largest audit and accountancy partnerships in the world.

Andersen was criticised for allowing its large-scale consulting business with Enron to influence its audit opinion. As a result of the scandal, the US Congress passed the Sarbanes-Oxley Act, which increased the accountability of auditing firms, demanding they be unbiased and independent of their clients. It also imposed additional penalties for destroying, altering, or fabricating records in federal investigations or for attempting to defraud shareholders.

The latest round of regulatory concern is related to the high-profile corporate collapses during the global financial crisis in Europe and the US.

Except for Deloitte, all the big four accounting firms spun off their consultancy practices, although most re-entered this market in 2004, but branded the work under their advisory engagements. None of them undertake big ticket computer implementation work, which was at the centre of

Andersen's so-called conflict of interest at Enron.

In Australia, consulting or advisory is a fast-growing area for the big four although audit remains the largest fee earner in dollar terms.

Deloitte has 700 people in consulting, up 20 per cent for the 2010-11 financial year. When Deloitte released its annual results in July, the firm stated that consulting services and its Deloitte Private division were the fastest growing practice areas.

PwC has around 800 staff while KPMG and E&Y have about 1000 each. Advisory was the largest contributor to E&Y's growth last financial year, up 29 per cent to \$255 million of total Australian fee income of \$1.05 billion.

Earlier this year, BDO, Grant Thornton, RSM International and Mazars in Europe called for intervention in the audit market.

"It's been acknowledged globally for some time that there is a lack of competition in a market dominated by the big four," said BDO's Tony Schiffmann, who predicted that whatever Mr Barnier achieved in Europe will influence other regulators.

"I think it will be significant and the general view of BDO and in my discussions with big four firms is that whatever is achieved in the European Union will impact global jurisdictions," Mr Schiffmann said.

Auditing and Assurance Standards Board chairman Merran Kelsall viewed any attempt to break up the big four as "a gargantuan task". Besides overcoming opposition from vested interests, any subsequent legislation would have to be passed by EU member states as well as the EU.

The big four firms would argue that creating pure audit practices would deprive them of the expertise of specialists in areas such as tax, and valuations that could add to the cost of auditing global firms.

"Quality audits need that expertise which is why they are in-house," E&Y assurance leader Tony Johnson said.

While acknowledging that legislation based on the Barnier proposals would inevitably put pressure on other jurisdictions to adopt similar laws,



EU commissioner Michael Barnier wants to limit audit practices.

Photo: REUTERS

Ms Kelsall questioned if the EU would back radical changes that lead to breaking up major firms. "You would question how well thought through these proposals are."

KPMG's national managing partner for audit, Duncan McLellan, described the proposed rules as "ill-conceived" and said they risk undermining audit quality rather than enhancing it.

In a statement Deloitte supported "proposals that would enhance independence, as well as measures that would contribute positively to the capi-

tal markets and support economic growth", but opposed joint audits, mandatory rotation and tendering, and a ban on non-audit services.

In Australia, the Treasury has released draft legislation designed to improve audit quality.

In a statement, Parliamentary Secretary to the Treasurer, David Bradbury, said the Corporations Legislation Amendment (Audit Enhancement) Bill would ensure that Australia's regulatory framework remains in line with "international best practice".

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Mentoring program

KPMG and Monash University's Asia-Pacific Centre for Science and Wealth Creation will provide a career mentoring program to students in Monash University's Master of Business (Science and Technology) program.

Ausenco wins study

Latin Resources has appointed Ausenco to make a scoping study on its Guadalupe Iron and Mineral Sands project in Peru.

Tax division appointee

William Buck has appointed Malcolm Wight, a director of tax services, to its tax division, which has 16 directors and 130 staff.

Fee for service endorsed

Joint Accounting Bodies (CPA Australia, the Institute of Chartered Accountants in Australia and the Institute of Public Accountants) has voiced support for the second tranche of the Future of Financial Advice reforms, which it said reflected its view that fee for service was in the best interests of client and financial planner.

Workers less confident

Global human resources firm Randstad's latest labour mobility index shows Australian workers' confidence about finding a new job has fallen to its lowest level in a year.

Tax loss reform backed

The Institute of Public Accountants has backed the government's stated intention to improve treatment of business tax losses. Currently, when a company incurs a tax loss there is no automatic refund of tax paid. The IPA wants companies to be able to carry back revenue losses.

Smartphone platform

Fortescue Metals Group is now using Deloitte's Bamboo smartphone platform, which stores continuity management procedures and action plans on employee mobile devices.

Barangaroo consultant

Barangaroo developer and design and construction project manager, Lend Lease, has appointed engineering consultancy Norman Disney & Young as lead services consultant.

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