AccountancyAge

Firms get strategic in lining up audit targets

by Richard Crump 16 Oct 2013

AUDITORS will need to become more strategic in how they recruit, allocate resources and manage their cost base in the wake of the Competition Commission's reforms to the large-listed audit market.

FTSE 350 companies must now allow accountants to compete for their audit work at least once every ten years, with organisations that tender less frequently than every five years being forced to report in which financial year audit engagements will be put out to tender.

Though less draconian than its earlier five-year tendering proposals, which were criticised as disproportionately costly - PwC estimated it would cost auditors and clients £52m a year - the commission guidelines will increase auditors' cost bases.

"There are multiple layers to that challenge," explains Hywel Ball, managing partner, assurance, at EY. "We will have to embed the cost of business development, tendering and transition into our business model."

Firms already expect a slew of audit tenders to come onto the market as a result of ten-year 'comply or explain' tendering guidelines introduced by the FRC last year, with David Sproul, Deloitte's senior partner and CEO, suggesting "something like 45 FTSE 100 audit tenders will come out within the next three years".

Gearing up

It is unclear whether the Competition Commission's guidance will change the number of tenders up for grabs in the near term, and firms will have to "look at what happens in practice as to whether companies stick to the FRC guidelines", says David Barnes, managing partner for public policy at Deloitte.

In either scenario, firms will need to selective over which clients they bid for. "In the last 12 months we have made plans and decisions as to whether there are companies we will look to target," says Barnes.

Deloitte are hardly alone in gearing up for the new environment. Indeed, Mazars' UK head of public interest markets, David Herbinet, says the firm has set up a number of initiatives to "build relationships and credibility" - such as its Centre for Audit Committee & Investor Dialogue, launched last year with three institutional investors.

Most important for firms that want to build relationships with prospective clients is the requirement that audit committees announce when they intend to tender. "Clearly that disclosure is extremely useful," says Herbinet.

To a certain extent, companies in the FTSE 350 have already started to disclose their intentions in their annual reports - National Grid, for instance, announced in its latest report that it would tender the audit by the time of its next audit partner rotation, currently scheduled for March 2015.

Tony Cates, head of audit at KPMG, agrees the five-year disclosures will give firms a "line of sight" and make the announcements "more crisp". "They can be a bit vague," he says. "Now you have to really allocate resource and target those companies."

Cates expects most companies will "go early" and hold a tender process before the ten-year period is up. James Roberts, BDO's audit partner, agrees with Cates that waiting until the end of the cycle will be "too risky" because of the potential for unforeseen events - such as the finance director resigning - and that most tenders will take place in years seven and eight.

"Everyone will need to think more strategically and go and self-select when they don't want to play," Roberts says, adding that he expects BDO to build on its TMT and retail sectors, among others. "It is quite important we say ‘this is an area we are focused on and do well in' and spend money and get the right people in."

Resource allocation

Indeed, others are predicting greater movement of people among the main players as firms look to bulk up on talent in areas they want to target, or areas where a clutch of audits are known to be coming to market.

"You get may get greater movement of partners between firms, if you are stronger or weaker in certain sectors," explains Cates.

Similarly, Ball at EY expects to see "more mobility in the workforce" as firms use their global capabilities to redeploy staff, while more "sector specialists with a finance background" could be recruited direct from industry. However, he doesn't expect whole teams to move within the profession and any raids among rivals will be "piecemeal".

But Barnes at Deloitte thinks such recruitment policies will be challenging. "In terms of bringing people from outside...it may prove challenging" to lure them away from industry and back into the profession, while poaching audit engagement partners will be "more difficult" than before.

"If you know that the audit is coming up you would not be able to take the engagement partner," he says. Instead, firms will redeploy their resources based on pre-existing relationships.

"If you look at most of the major companies we want to have a relationship with them in one form or another. It is a question of redistributing resources to build relationship between audit and finance instead of areas like tax," he says.