

## ***Workshop 2 – Networks and Networking***

***Friday 8th September 2006***

***9:00 to 10:30***

### **Facilitator:**

***José Maria Bové, FEE Vice-President & SME/SMP Working Party  
Chairman***

FEE Annual European SME/SMP Congress, Palais des Congrès, Versailles, France, 7th & 8th September 2006

## ***Workshop 2 – Networks and Networking***

***Friday 8th September 2006***

### **Speakers:**

***David Chitty, Vice-Chairman Practice Advisory Board & Council Member of ICAEW,  
Partner Chantrey Vellacott DFK, UK***

***Hervé Puteaux, Partner JPA, France***

***Peter Galambos, Hungarian representative FEE Working Party, Partner, Mazars Metrum  
Ltd, Hungary***

***David Maxwell, Chairman of European Grouping of International Accounting Networks  
(EGIAN)***

***Jeremy Jennings, Chairman of European Contact Group (ECG)***

***Anne-Françoise Mélot, Auditing Unit, DG Internal Market, European Commission***

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**FEE SME/SMP CONGRESS**  
**Versailles, 7-8 September 2006**  
**Networks and Networking**

**David Chitty**

**Vice-President, Europe, Middle East &  
Africa, DFK International**

**ICAEW Council Member**



**UK tradition**

- Foundation stones of many of the current international groups were laid in the UK
- Technical and training support
- Marketing groups
- Principles versus rules-based approaches



## US

- Rules-based tradition
- Liability and branding links
- Independent approach by firms
- Local market emphasis
- State licensing



## Interpretations

- National interpretations may vary
- EU/Non-EU
- National differences
  - Independence rules and penalties
  - Multi-disciplinary versus auditor-led approaches



## **Working together**

- Consistency of regulations and standards
- Agreement on quality
- Smoothing cultural issues



## **FEE SME/SMP CONGRESS Versailles, 7-8 September 2006 Networks and Networking**

**David Chitty**

**Vice-President, Europe, Middle East &  
Africa, DFK International**

**ICAEW Council Member**



# **Networks and Networking: Impact of the New Company Law Directive on Statutory Audit**

**FEE/AMA SME/SMP Congress**  
**« Growing Businesses in a Changing Global Environment »**  
**Versailles, 8 September 2006**

*Anne-Françoise Mélot*  
*European Commission*  
*Policy Officer*

Internal Market & Services DG

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## **Outline of the presentation**

1. New Directive 2006/43/EC on statutory audit
  - Timing and state of play
  - Key points
2. Network definition
3. Practical implications
4. Future developments

Internal Market & Services DG

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## 1. New Directive 2006/43/EC on statutory audit: timing and state of play

- Replaces the Directive 84/253/EEC of 10 April 1984
- A comprehensive, principles based Directive
- Entry into force: 29 June 2006
- Transposition by Member States into national law: **30 June 2008** (2 years)

## New Directive on statutory audit: key points

- Approval, ownership and registration of statutory auditors and audit firms
- International Standards on Auditing (ISA)
- Ethics and Independence
- Quality assurance and public oversight
- Specific requirements for the audit of Public Interest Entities
- International dimension

## 2. Network definition



- **Article 2, paragraph 7:**

“Larger structure aimed at cooperation to which a statutory auditor or an audit firm belongs

and

which is clearly aimed at profit- or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, a common business strategy, the use of a common brand-name or a significant part of professional resources”

- **IFAC revised definition** (July 2006) aligned on Audit Directive

## 3. Practical implications

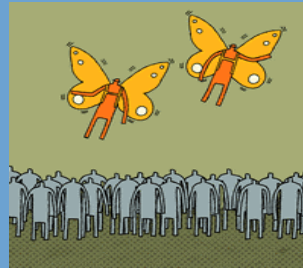
- **Registration of audit firms (Article 17 (h))**
  - public register shall contain the **membership of a network** and a list of the **names and addresses of member firms** and affiliates or an indication of the place where such information is publicly available



### 3. Practical implications

- **Independence and objectivity** (*Article 22 and recital 11*)

- statutory auditor and/or audit firm:
  - independent of the audited entity
  - not involved in the decision-taking of the audited entity



### 3. Practical implications

- *Article 22*

- no direct or indirect financial, business, employment or other relationship (including the provision of additional non-audit services) between the statutory auditor, audit firm **or network** and the audited entity
- from which an objective, reasonable and informed **third party** would conclude that the statutory auditor's or audit firm's independence is compromised.



### 3. Practical implications

- *Recital 11*

Public oversight should take all circumstances into account, such as « **common usual clients** »

### 3. Practical implications

- **Transparency report** (*Article 40*)

- Who: Auditors/audit firms of public interest entities
- What: description of the network and its legal and structural arrangements
- Where: Publication on the website of the audit firm
- When: within 3 months of the end of each financial year



## 4. Future developments

- **Transposition of the Directive**

- Need for clarity and consistent interpretation and application of the definition across EU
- Transposition workshops with Member States (start: November 2006)
- No comitology measures on networks

## Transposition of the Directive (cont'd)

- Indirect benefit: mutual recognition
  - **Ownership** and **management** requirements
  - Natural persons carrying out statutory audits on behalf of the firm: approved as statutory auditors in Member State of the firm
  - Equivalence of audit qualifications, but **aptitude test**
  - **Home country control** and oversight by the Member State in which the auditor is approved

# Future developments

- **Markets**

- Trade off investors/auditors: Importance of the brand
- UK debate: competition and choice
- EC future study on ownership
  - Contractor to be selected and to start in the autumn
  - Objective: to determine, under the limits fixed by the new 8th Directive, the link between ownership rules/voting rights applying to the audit firms and the concentration on the market for the audit of financial statements of public interest entities

# Future developments

- **Auditor's Liability**

- Study from London Economics, commissioned by EC, on the economic impact of auditors liability regime: to be published beginning of October
- Commission report (Article 31 of the Directive) by the end of the year
- Issues linked to network to be addressed in the study:
  - Possible disappearance of a big network?
  - Concentration
  - Mergers and acquisitions amongst networks
  - Barriers to entry for smaller networks

## Further information

Visit us!

DG Markt website:

[http://europa.eu.int/comm/internal\\_market/en/company/index.htm](http://europa.eu.int/comm/internal_market/en/company/index.htm)

Contact us!

[Markt-F4@ec.europa.eu](mailto:Markt-F4@ec.europa.eu)

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## Networks & Networking

The relationship between networks and auditor  
independence - a large firm perspective



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## 8th Directive – definition revisited

- Larger structure aimed at cooperation, **and**
- Clearly aimed at profit/cost sharing, **or**
- Common ownership, control, management
- Common quality control policies & procedures
- Common business strategy
- Common brand name
- Use of significant professional resources
- Recital reference to “common usual clients”

From an ECG perspective, not much cause for concern.



## The network – practical challenges

- Compatibility with the IFAC definition – similar but takes a slightly different approach:
  - Common control, ownership or management, or
  - Reasonable and informed third party test
- Monitoring independence compliance:
  - The effect of “extra-territoriality”
  - Lack of materiality and de minimis provisions
  - Internal pressures: audit or non-audit?
  - Incentives to move towards a “regional” structure



## The Network Dichotomy

A. In theory, a more centralised network leads to greater consistency in application of audit methodology and quality, but

B. In theory, the more centralised the network, the greater the liability risk that the “failure” of a local practice will infect the international organisation

If regulators and other stakeholders want “A”, then there needs to be a general acceptance that “B” has to be fixed.



## Impact of network definitions on middle sized networks

David Maxwell of RSM International  
Chairman of EGIAN

**EGIAN**

**EGIAN**

European Group of International Accounting Networks

- ◆ Representing: 20 networks
- ◆ European fees €5bn
- ◆ People in Europe 65,000

**EGIAN**

## Impact of network definition

- ◆ Brings clarity into grey areas and thus:
  - Defines market segments
  - Forces a strategic decision by networks

**EGIAN**

## Strategic decision

**International**  
service provider

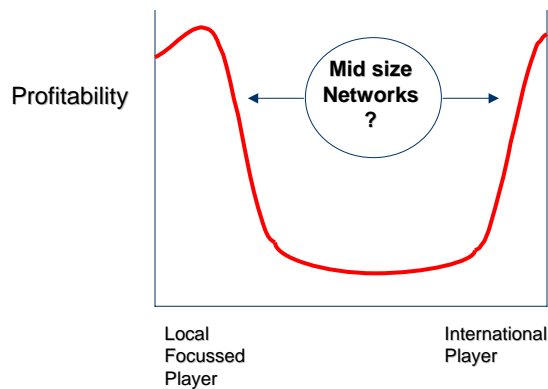
or

**Local**  
player

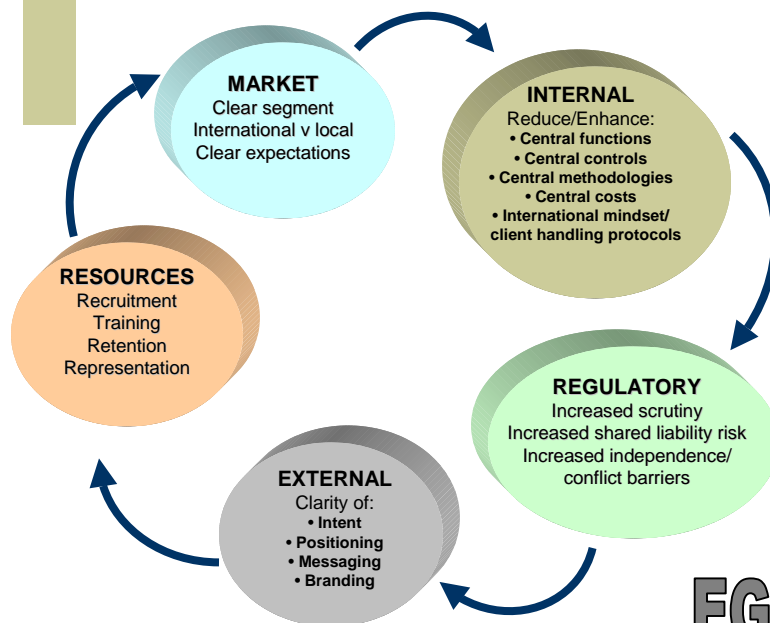
**EGIAN**



## Valley of death



EGIAN



EGIAN

# International Networks in Hungary

Péter Galambos  
Partner  
Mazars Metrum (Hungary)

# International Networks in Hungary

- Auditing, as a new activity
- SME-s in Hungary and the structure of the audit profession
- Local international networks in Hungary
- Aspects for selecting a network

## Auditing as a new activity

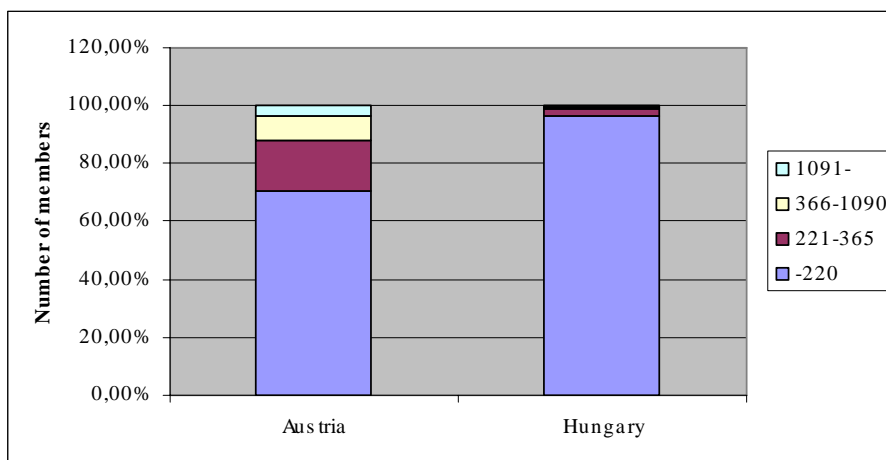
- Resumption of auditing in 1988
- Chamber Act 1997
- Study process

## SME-s in Hungary

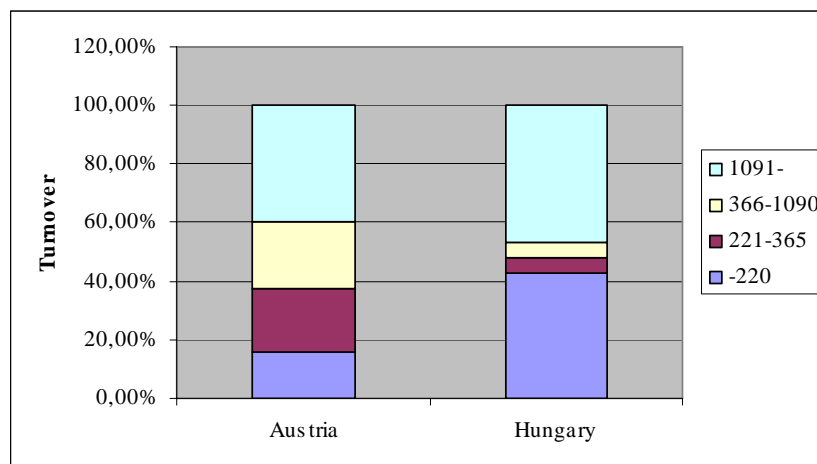
In comparison to the EU average:

- Higher number of firms (61 – 49 firms / 1000 capita))
- Smaller average company size (5 – 7 employees/firm))
- Less mid-size companies
- Low audit limit

## Percentage distribution of the audit companies by their number



## Percentage distribution of the turnover of the audit companies



## International Networks in Hungary

- Establishment of own firms
  - Big 6
  - French companies
    - Mazars, (Guerard Viala, Salustro Reydel)
  - Austrian and German firms
    - Creation of local networks
- Successful strategy

Enterprise	Seat of parent company	Hungary	Czech Republic	Slovakia	Slovenia	Croatia	Poland	Ukraine	Romania	Membership in intl. network
<b>Consultatio.</b>	Austria	X	X	X	X					AGN
<b>Leitner + Leitner.</b>	Austria	X	X	X	X	X				-
<b>IB Grant Thornton.</b>	Austria	X	X	X	X	X				Grant Thornton
<b>TPA Horwath</b>	Austria	X	X	X	X	X	X			Horwath
<b>Rödl und Partner</b>	Germany	X	X	X	X	X	X	X		CPA
<b>Haarmann-Hemmel</b>	Germany	X	X				X		X	RSM

## International Networks In Hungary

- 21 from the largest 25 networks present(Accountancy 2006 June)
- Czech Republic 16, Poland 15, Slovakia 14

## Aspects for selecting a network

What is most important:

- Turnover or
- Other factors:
  - Personal relationship
  - Acquisition of professional know-how
  - Development of methodology
  - Further training of staff

## **NETWORKS AND NETWORKING**

### **PRACTICAL EXPERIENCE OF NETWORK**

Hervé PUTEAUX  
Expert-comptable  
Commissaire aux comptes  
CEO JPA INTERNATIONAL  
Paris, FRANCE

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### **PRACTICAL EXPERIENCE OF NETWORK**

#### **CONCEPT:**

A network dedicated to provide the best services for clients in any professional areas respecting our professional regulations

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## PRACTICAL EXPERIENCE OF NETWORK

The members of a network: which profile?

-A Charter to ensure basic key points:

- Honesty
- Integrity
- Professionalism

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## PRACTICAL EXPERIENCE OF NETWORK

The members of a network: which profile?

-A Quality control process

- General organization, Activity, Human resources, Procedures of working, Fees, Insurances, Data processing system,...

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## PRACTICAL EXPERIENCE OF NETWORK

The members of a network: which profile?

-A final choice:

- The potential member has an interest for international needs
- And/or the network has an interest in a particular country, city, skill.

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## PRACTICAL EXPERIENCE OF NETWORK

Practical organisation:

- A Chairman,
- Continental Vice-Presidents,
- A CEO,
- A Board,
- The members.

A global process based on personal and close relationships between members is a key to success.

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## PRACTICAL EXPERIENCE OF NETWORK

### Practical organisation:

-2 major areas:

- 1. The technical and supporting area
- 2. The business area

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## PRACTICAL EXPERIENCE OF NETWORK

### Practical organisation:

#### **-1. The technical and supporting area**

- Quarterly meetings
  - network improvements and developments, technical commissions (IFRS, ISA's, EU regulations, Tax...), external speakers, cross border services developments, communication, quality controls reports, skills databases...
- Regular conferences and training for members staff
  - Internal control,
  - IFRS
  - IFAC standards,
  - EU Directives...

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## PRACTICAL EXPERIENCE OF NETWORK

### Practical organisation:

#### **-2. The business area**

- Network promotion
  - Embassies, Chambers of commerce, prescribers (banks, lawyers,...), professional documentation,...
- Promotion of particular local attractive facts (foreign investments, holding matters, ...)
- Continental meetings to promote the synergy between members (Asian, European, American, Middle eastern... approaches)
- Coordination and support for cross border services (client support, translation, technical support...)