



# DYNAMICS INFLUENCING AUDITOR CHOICE IN THE PUBLIC INTEREST ENTITY MARKET

AUDIT & ASSURANCE

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## BACKGROUND

Auditing public interest entities (PIEs), ranging from banks and large international companies to smaller and locally listed companies, requires significant resources and skills and is highly regulated. The public interest demands a diverse and resilient statutory audit (hereafter 'audit') market with enough audit firms active in it. This ensures that the needs of all PIEs and their stakeholders are served.

The limited choice of audit firms and concentration in the PIE audit market are interlinked topics that have been attracting a lot of attention from stakeholders such as academics and policymakers. [Our publication](#) contributes to this complex debate. It focuses on the aspect of auditor choice and looks at the matter in a holistic way, considering the interconnected key parties and factors that influence auditor choice. Here, the term *auditor choice* refers to the pool of audit firms that PIEs assume they can choose from<sup>1</sup>. It is influenced by the below listed key factors related to the demand- (PIEs) and supply-side (audit firms).

The four main parties in this equation are companies, including their audit committees and shareholders, auditors, policymakers and public audit oversight bodies. Understanding how they influence auditor choice is crucial to recognise what encourages, and what negatively impacts, auditor choice in the PIE market.

## OBJECTIVE

Our publication aims to:

- provide insight to policymakers about the dynamics and challenges in the PIE audit market that have led to its current structure and to the PIEs' limited choice of audit firms. This includes looking at key factors that influence how PIEs choose their audit firm and how audit firms decide about their involvement in the PIE audit market
- present our ideas to promote auditor choice and make PIE audits more attractive
- lay the grounds for further discussion with all stakeholders, including policymakers

Policymakers should not underestimate the challenges audit firms face when attempting to move into, or expand in, the PIE audit market. This is especially relevant when considering the future of the audit market and in the context of the [European Commission's initiative on corporate reporting](#). Impact assessment of any measure will be necessary to inform any policy making.

<sup>1</sup> There are two other matters that this publication does not focus on but clarifying them may be useful for the reader:









1) *Market concentration* in the PIE audit market: European PIEs' auditors are predominantly Big 4 audit firms as explained in the [publication's](#) section *Today's audit market and its evolution*

2) *Competition*, i.e. the degree of competition amongst audit firms in the (PIE) audit market







## KEY FACTORS DETERMINING AUDITOR CHOICE IN THE PIE AUDIT MARKET

We identified, through discussions with our audit experts and outreach with stakeholders, the key factors that influence i) how PIEs choose their auditor and ii) how audit firms decide on their involvement in the PIE audit market. PIEs and audit firms generally consider the respective factors together, but some factors may play a bigger role than others, depending on the circumstances.

### DEMAND SIDE: WHICH FACTORS DO PIEs CONSIDER WHEN CHOOSING THEIR AUDITOR?

	reputation as proxy for capability and quality
	experience
	international presence
	audit approach and strategy
	capacity to provide assurance services
	making a 'safe' choice
	regulatory compliance: rules on tackling conflicts of interest and audit firm rotation
	price

### SUPPLY SIDE: WHICH FACTORS DO AUDIT FIRMS CONSIDER WHEN DETERMINING THE EXTENT OF THEIR INVOLVEMENT IN THE PIE AUDIT MARKET?

	regulation, including rules on: tackling conflicts of interest, mandatory audit firm rotation, and insurance and liability costs
	audit oversight
	commercial aspects
	human aspects and attractiveness
	level of integration within an audit firm network
	risk management and audit quality

## EXPLORING HOW TO PROMOTE AUDITOR CHOICE AND MAKE PIE AUDITS MORE ATTRACTIVE

Our publication presents the ideas below as a step in the right direction to promote auditor choice and make PIE audits more attractive. This is not straightforward, and none of these can be a standalone solution. The matter of auditor choice requires a holistic approach, building on different measures which address both demand and supply side issues. We invite policymakers to consider these ideas holistically, including any challenges that they may bring.

Making PIE audits more attractive will require a combination of efforts by all parties, including:

- **change of mindset** – companies with their audit committees and shareholders, policymakers and audit supervisors need to be more open to enable and support diversity in the PIE audit market
- **enhancing corporate governance** – measures to further improve the quality of financial reporting and mitigate corporate risks will help with de-risking PIEs, thus allowing them to find an auditor more easily
- **enhancing the auditor selection process** through:
  - ensuring audit committees' consistent approach in this process
  - strengthening shareholder engagement in the auditor selection
  - consistent oversight of audit committees
  - enhancing transparency of audit oversight bodies' work to help bridge the information gap on audit firm quality. This will ensure that audit committees have access to reliable information on quality when selecting an audit firm
- **lowering the existing barriers**, especially in regulation, and avoiding the creation of new ones as they add costs and disincentivise audit firms from joining the PIE audit market. This involves the need for:
  - consistent and proportionate audit rules and oversight across countries
  - continuing to allow assurance services, linked with the audit, to audit clients – this will avoid further reducing the number of auditors available to PIEs
  - proportionate liability regimes for auditors
- **strengthening the educational dimension of audit oversight** to help foster learning and development of the audit profession and enhance the quality of audits
- **creating a PIE audit market environment that is an attainable and attractive** proposition for new entrants, including policymakers exploring ways to help mid-tier audit firms win PIE audit clients
- **capacity and expertise building**, especially in mid-tier audit firms as potential entrants to the PIE audit market

## CONCLUSION AND NEXT STEPS

Further research on the EU audit market is needed to clearly define the issues and explore existing barriers to more auditor choice, the appetite of audit firms to audit PIEs and PIEs' appetite to appoint mid-tier audit firms as their auditor. Gathering facts and stakeholders' input are crucial to inform any future policy making.

Looking forward, and at the wider market, it will be interesting to see the implications of sustainability assurance on choice and selection of auditors and sustainability assurance providers. What is clear for now is that with the newly required sustainability assurance, having more capacity in the audit market as a whole becomes even more relevant.

We believe that the only way forward is to continue discussions with stakeholders, as we have done through outreach when developing this publication. In this spirit, we will hold an event to enable a public dialogue in the coming months.