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Dear Mr Gadhia

Audit Market Investigation
KPMG Response to "Barriers to Entry: International Networks" Working Paper

This paper provides our response to the CC's Working Paper on "Barriers to Entry: international networks" (the "Working Paper"). We welcome the chance to comment on this Working Paper, and look forward to continuing to engage with the CC on this topic.

In our response to the CC's Working Paper "Restrictions on entry and expansion" we set out our views on the CC's approach to assessing international networks as barriers to entry. Audit firms serving clients with international operations need to respond to the demands of those clients for an audit firm with a high quality international network in order to retain those audit clients. Similarly, member firms join strong international networks because it gives them confidence that high quality services will be delivered to their own clients outside of their own jurisdiction.

We disagree that international networks can be characterised as barriers to entry; they are simply responses to client demands and competitive pressures. In addition, the mid tier firms have strategies available to them to gain coverage and skills, including expanding their networks, adopting better centralised co-ordination, planning and controls, and targeting specific countries to strengthen their global presence.

We set out in the appendix our detailed comments on the Working Paper.

We trust that these comments and observations are useful in informing your consideration of the Working Paper. Do not hesitate to contact me if you have any queries or wish to pursue any of these points further.

Yours sincerely

David L Gardner
Director of Public Policy

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Appendix 1

Unless otherwise stated, paragraph references are to paragraphs in the Working Paper

WP paragraph	**KPMG comment**
38	There are very few recent examples beyond the two cited in the House of Lords Economic Affairs Committee report, of smaller national firms choosing to join larger audit firm networks. As in Brazil, in these rare cases national firms may feel that they require broader and deeper capability in a global network as their audit clients globalise and expand. While consolidation has been market driven by clients' requirements, drive to meet clients needs have also resulted in national firms moving away from the larger networks to mid tier networks where they feel it better sits with their strategy and client base, such as SAB in Belarus which recently left the KPMG International network in November 2010 to join BDO International[1]
39	This evidence supports our view that audit firms' expansion of their international networks is driven by client demand and for global quality and consistency throughout the international markets of the audit client's operations– where a member firm fails to deliver the quality standards we require of them to meet our clients' expectations, or there is a lack of demand, that member firm may be removed from the network.
41	As we stated in our response to the CC's working paper "Firms' Stated Competitive Strategies", the principal purpose of establishing our KPMG Resource Centre (KRC) and KPMG Global Services Centre (KGS) is to further improve our ability to deliver high quality service to our clients, and not simply to reduce cost. KRC and KGS provide our onshore professionals (in whatever country) with high quality, globally consistent support. KRC and KGS also substantially extends the effective KPMG working day. The scale and quality of KRC and KGS professionals enables high quality data analysis and other audit activities capable of being done remotely to be handled in an efficient and consistent high-quality manner. As a result, our onshore professionals (in whatever country) now focus more time on higher qualitative aspects of the audit, resulting in a more efficient process. [2]
49	We agree that it could be an advantage for a resource centre to work in partnership with a local member firm to leverage their knowledge and capabilities to provide support and quality assurance. However, we note that 23 of the 24 forum of Firms network members have member firms in India, the dominant location for such offshoring for UK purposes, and would therefore have the local supervisory capability should they choose to operate a shared service centre in that territory. [✂]
50	Please see our response to paragraph 41 above.
57	The CC's reference to Mazars having strategic focus in terms of targeting clients and sectors shows that mid tier firms can (and do) plan centrally. There is no reason why mid tier firms cannot deploy targeting strategies to grow their businesses, as we discuss further in our response to the CC's working paper on "Barriers to entry: reputation and

[1] [✂]
[2] See our comment in response to paragraph 17

WP paragraph	KPMG comment
	experience".
74	The CC asserts that £250 million (which is what one firm spent on developing a global audit software platform) is too great an investment cost for a single firm to bear. Firms with international networks can spread these costs over the whole network and benefit from economies of scale. It is noticeable from the Annual Reviews and transparency reports from other networks beyond the largest four that they have also invested very heavily globally in global audit methodologies (and IT tools to support it), client and engagement acceptance, audit quality reviews and international standards' groups (on IFRS, ISAs etc.) to support national member firms[3].
81 - 102	Our international network is driven by client needs. This includes both representation and capacity within a country. The CC states that individual member firms of the smaller networks may 'potentially have less capacity to resource engagement teams for large subsidiaries at short notice'. We agree that small offices might have limited capability to service international referrals, particularly if much of the internationally referred work occurs in (eg) Jan for (eg) Dec year ends. However, with good planning, effective global mobility and strategic focus, smaller networks should have the capability to deploy teams for specific FTSE350 companies operating internationally. This is not a 'barrier to entry' in the sense of it having an adverse effect on competition, rather it is a response to competitive pressures and client demands. The mid tier firms can and are expanding and developing their international networks, also in response to client demands.
113	The CC concedes increased client demand for international audit services makes it "increasingly important for an audit firm to have a suitable network to deliver this work". As we have consistently stated, international networks are a function of client demand.
115	Whilst the CC considers whether aspirations to expand overseas would prevent those UK companies from using a firm with a less developed international network, we note that "only 8 per cent" of respondents from UK-only companies considered international network to be important when choosing an audit.
126 (e)-(f)	To the extent that there are any inaccurate perceptions about the mid tier firms in the market, there are strategies available to the mid tier firms to increase their communication and awareness, including through specific targeting. We discussed these strategies in more detail in our response to the CC's working paper on "Barriers to entry: reputation and experience."

[3] See, for example, BDO Annual statement http://viewer.zmags.com/publication/f512b3bc#/f512b3bc/1 and Grant Thornton International transparency report http://www.gti.org/Transparency-report/index.asp

WP paragraph	**KPMG comment**
128	The CC states that "strategic objectives..... may affect..... the level of profit a member might extract". As we have consistently stated, the drivers for developing an international network are client demands and competitive pressures. It is not simply about the profit, but about increasing the quality and product to the clients. Although there are certain benefits associated with the network, it is driven by client demand.
128(b)	The activities the CC refers to in this paragraph are evidence of the sorts of actions audit firms take to increase efficiency and provide a better service to clients, in response to client demands and competitive pressures. Further, mid tier firms can, and do already, take advantage of this. This is therefore not a barrier to entry.
128 (c)-(d)	The CC does not provide any evidence to back up the statements made in these sub-sections, in particular in relation to sub-section (d). We discuss reputation in more detail in our response to the CC's Working Paper "Barriers to Entry: reputation and experience".