



Meeting: Stakeholder Advisory Council (SAC)
Meeting Location: New York
Meeting Date: November 4-5, 2024

Agenda Item **3**

Future of Accounting Firms

Introduction

1. At the April 2024 SAC meeting, Members provided valuable insights on the topic of Firm Culture and Governance (FCG). These insights have been considered by the IESBA as it continued with its information gathering under the FCG work stream in quarter 2 and quarter 3. During the first part of the session, SAC Members will be asked to provide strategic advice on how the IESBA should approach the next phase of this initiative to ensure impactful and globally relevant outcomes.
2. Another issue that has emerged, with potential impact on firm culture, is the growing trend of private equity investments (PEI) in accounting firms. During the second part of the session, International Federation of Accountants (IFAC) Director David Madon will highlight the research and analysis conducted by IFAC with respect to PEI in accounting firms. SAC Members will then break into groups to discuss the potential implications of PEI in accounting firms relative to three fundamental themes – public trust, audit quality and independence, and governance and oversight. Please refer to the allocation of the breakout groups in **Appendix 1**.

Part A – Charting A Path Forward on Firm Culture and Governance

3. At the September 2024 IESBA meeting, the FCG Working Group (FCGWG) presented its [Preliminary Report](#) for the IESBA’s consideration. The IESBA was generally supportive of the Working Group’s preliminary views and recommendations (see Executive Summary and Sections VIII and IX of the Preliminary Report). In reaching its views, the FCGWG has taken into account feedback from stakeholders, reviewed jurisdictional audit firm governance codes as well as considered the role and impact of the IAASB’s ISQM 1 on firm culture.¹
4. As the FCGWG prepares its final report and develops a project proposal for the next phase of this initiative, it seeks the SAC’s strategic advice on shaping the long-term objectives, scope, and priorities of the Working Group’s recommendations to the IESBA to undertake a standard-setting project and develop non-authoritative material.

¹ International Standard on Quality Management (ISQM) 1 deals with a firm’s responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements. The IAASB published the standard in December 2020, with firms required to have their system of quality management designed and implemented by December 15, 2022.

The Influencing Factors of Ethical Leadership and Governance

5. Stakeholders generally agreed that a strong ethical culture would help firms mitigate the risks of unethical behavior and enhance their reputation. An ethical culture is crucial not only for building public trust but also for positioning ethics as a long-term value proposition. By embedding ethics at the core of their strategies and operations, firms can differentiate themselves in the market, assuring investors and other stakeholders of consistent, trustworthy performance and sustainable growth for clients over time.
6. Through its information gathering, the FCGWG has identified ethical leadership and effective governance as two key influencing factors of ethical culture within an organization. The Preliminary Report highlights the need for firms to treat ethical leadership as more than just a compliance obligation, positioning it instead as a key driver of business sustainability and investor protection. Moving beyond the view of ethics as a regulatory checkbox, firms should see integrating ethical leadership into their business models as a strategic imperative. To put it simply, firm leadership should view ethics as a key condition to success.
7. To develop a strong culture that promotes ethical practices, the FCGWG also recognized the importance of embedding ethics into a firm's broader governance structure. Such a structure may include measures such as independent non-executives, an accountability mechanism, non-financial performance metrics, and public disclosure of ethical performance.

1. *At a strategic level, besides ethical leadership and governance, are there any other dimensions that also have a substantive impact on a firm's ethical culture?*

The Recommended Role of Standard-Setting

8. The preliminary report presented two preliminary recommendations for IESBA to consider as the way forward:
 - (a) Development of new standards that set a global baseline for how firms should address leadership and key elements of an ethical governance framework.
 - (b) Development of non-authoritative guidance material which, amongst other things, would highlight the importance of a strong ethical culture, what an ethical firm looks like, and, through the development of a framework, the roles of key stakeholders in promoting ethical behavior and a strong ethical culture within firms.
9. The FCGWG also proposes that these two recommendations be implemented concurrently, commencing with a series of global roundtables in early 2025. The FCGWG's recommendations and approach recognize a need within the ecosystem for robust principles-based standards that set a global baseline while acknowledging the role of other players, such as regulators, investors, the corporate governance community and professional accountancy bodies, in promoting ethical practices in firms.

2. *From the perspective of investors, users, or the accountancy profession, what specific challenges or risks do you foresee in the implementation of the FCGWG's two recommendations? How can these challenges or risks be mitigated to ensure success in implementing the recommendations?*

Part B – Impact of Private Equity on Firms

10. Historically, accounting firms operated under partnership or limited company structures due to regulatory requirements or other factors. One economic challenge of partnership models or any cooperative scheme is that the ability to accumulate capital for investment depends on retained earnings. This economic reality can impose limits on the potential for transformational investment or the ability for new competitors to emerge.
11. The use of private equity funding marks a shift in both the ownership and legal structure of accounting firms. Typically, PEI introduces outside investors and requires legal restructuring of firms, resulting in two entities: the audit and assurance practice (exclusively owned by Certified Public Accountants) and a separate company that performs non-assurance services offered by the firm. Private equity investors would be able to invest in the separate company, while CPA partners would retain an ownership interest in the new non-assurance entity.
12. The PEI trend² has been on the rise in the United States and the United Kingdom (UK) and is gaining popularity in several other jurisdictions. For example, several private equity firms are competing to invest up to £1.5bn in a mid-tier UK accounting firm.³ Also, a recent study by the Institute of Chartered Accountants in England and Wales⁴ found that 12% of respondents had already secured PEI, and another 12% were likely to secure PEI in the next three years. Of those who had secured funding, 80% did so within the last three years.
13. Private equity structures can be complex and include varying levels of influence over other entities. Significant changes within an accounting firm can influence leadership and culture. Altering the ownership structure through external private capital may threaten the critical public interest aspect of financial statement audits as well as a firm's consulting and advisory services, given the primary objective of PEI on profit maximization. Firms must be prepared to uphold statutory independence requirements and address conflicts that may threaten independence, integrity, and the quality of the services provided.
14. The trend toward PEI in accounting firms has alerted regulators to potential impacts on independence and audit quality.⁵ As a result, the United States Securities and Exchange Commission and the UK Financial Reporting Council,⁶ as well as other regulators such as the International Organization of Securities Commissions, are closely monitoring this activity. When accounting firms consider obtaining PEI, attention should be given to the implications these structures may have on compliance with independence requirements⁷ as well as audit quality standards.

² The rise of private equity in accounting: Not just for large firms anymore <https://www.thomsonreuters.com/en-us/posts/tax-and-accounting/private-equity-accounting-firms/#:~:text=In%20less%20than%20three%20years,are%20attractive%20to%20PE%20investors.>

³ [Private equity circles Grant Thornton's UK business \(ft.com\)](#)

⁴ Here's how mid-tier accounting firms are feeling about private equity and mergers and acquisitions <https://www.goingconcern.com/heres-how-mid-tier-accounting-firms-are-feeling-about-private-equity-and-ma/>

⁵ [Private equity's interest in audit raises red flags \(ft.com\)](#)

⁶ [UK accounting watchdog tells audit firms to report approaches from private equity \(ft.com\)](#)

⁷ Auditor independence and ethical responsibilities: Critical points to consider when contemplating an audit firm restructuring <https://www.sec.gov/newsroom/speeches-statements/munter-statement-auditor-independence-ethical-responsibilities-082922>

Breakout Group 1 – Public Trust

15. The integration of PEI in accounting firms introduces a complex dynamic that warrants a thorough examination of its potential impacts on the profession and beyond. As private equity firms infuse capital and business strategies aimed at enhancing growth and efficiency, they simultaneously raise critical questions about audit quality, independence, and overall integrity within the accounting sector. The nuanced balance between leveraging PEI for modernization and growth versus maintaining the ethical and professional standards that underpin public trust in the profession becomes a focal point of this conversation.

How can firms align their public interest responsibility with PEI's primary objective to maximize profit for investors?

Breakout Group 2 – Audit Quality and Independence

16. As noted previously, the increase of PEI in the accounting industry raises questions about its influence on audit quality and the overall integrity of the profession. Whilst private equity firms seek to invest in accounting firms as an opportunity to increase their profit by investing in businesses with high profit potential, accounting firms look at this type of investment as a lever for growth and modernization. Regulators are examining whether these investments may alter both the perceived and actual quality⁸ of audits performed and associated risks for the public interest that accounting firms are required to pursue. The accounting profession has been under increased scrutiny due to accounting failures, leading to reputational damage and trust erosion. Therefore, exploring the potential consequences of strategic alliances with private equity organizations is a critical component of risk assessment. In fact, due to their natural and exclusive focus on profit, the influence of PEI on the objectivity and integrity of professional accountants is an important factor, as it could jeopardize client trust and raise issues of perceived or actual threats to independence,⁹ which is foundational to the audit profession.

How might private equity investments in accounting firms affect quality management at the firm and engagement levels? Is it possible, in practice, to address the risks posed by PEI in accounting firms with respect to fundamental ethical principles and independence?

Breakout Group 3 – Governance and Oversight

17. Exploring the influence of PEI on constructs like firm culture, decision-making, and client relationships is essential when assessing the broader ramifications these types of structures have on the profession. Furthermore, as accounting firms navigate these changes, they must weigh the benefits of improved resources and resilience against potential conflicts of interest and independence threats. This examination sets the stage for a deeper dialogue into the strategic and ethical considerations that accounting firms must address as they evaluate the possibility of integrating PEI into their

⁸ The Accounting Review Registered Report Proposal: Does Private Equity Investment in Accounting Firms Affect Perceived and Actual Audit Quality? https://assets.pcaobus.org/pcaob-dev/docs/default-source/economicandriskanalysis/conference/conference---spring/session_1_borysoff_conaway_riedl.pdf?sfvrsn=78eec07b_1

⁹ The Critical Importance of the General Standard of Auditor Independence and an Ethical Culture for the Accounting Profession. U.S. Securities and Exchange Commission, June 8. <https://www.sec.gov/news/statement/munter-20220608>

operational frameworks.

How might PEI impact the ethical culture of accounting firms and how might firms manage such impact and ensure that the search-for-profit objective does not override the need to abide by strong ethics principles, independent practices and the public interest?

All Breakout Groups

18. In addition to the specific question for each breakout group above, Members will be asked to discuss the following common questions within their groups.

What impact will PEI have on the accounting practice market? What should the IESBA and IAASB be concerned about as standard setters beyond the matters already discussed in your group?

Way Forward

19. The IESBA staff will provide an update on the progress of the workstream, including feedback received from SAC members during this session, at the December 2024 IESBA meeting.

Material Presented

For Discussion

Agenda Item 3.1 Presentation: Future of Accounting Firms

For Reference

[Agenda Item 5A - Firm Culture and Governance Working Group Preliminary Report](#)

APPENDIX 1

List of Break-Out Groups

	SAC Member	Organization
Break-Out Group One: Public Trust (Orange Room)		
1.	Alan Johnson	SAC Chair
2.	Abdelilah Belatik	General Council for Islamic Banks and financial Institutions
3.	Chikako Matsumoto	Sumitomo Mitsui Trust Bank
4.	Ivanyra Correia	Board Member and Finance Executive
5.	Javier de Frutos	European Federation of Financial Analysts' Societies
6.	Jose Esposito	Banco de Credito del Peru / Credicorp Ltd
7.	Koichiro Kuramochi	Financial Services Agency
8.	Nicole Ratzinger-Sakel	University of Hamburg
9.	George Kabwe (Observer)	International Monetary Fund
Break-Out Group Two: Audit Quality and Independence (Green Room)		
1.	Dr Bello Danbatta Lawal	Islamic Financial Services
2.	Doug Niven	Auditing and Assurance Standards Board
3.	Hilde Blomme	Accountancy Europe
4.	Hina Usmani	Usmani & Co.
5.	Iheanyi Anyahara	Financial Reporting Council of Nigeria
6.	Steven Lipiner	PIMCO
7.	Toshimitsu Suzuki	Daiwa Institute of Research Ltd.
8.	Vicki Myburgh	PwC
9.	James Ferris (Observer)	Financial Reporting Council
10.	Robert Buchanan (Observer)	PIOB Observer
Break-Out Group Three: Governance and Oversight (Virtual)		
1.	Ashley Rangel	US Office of the Comptroller of the Currency

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	SAC Member	Organization
2.	Claes Norberg	Confederation of Swedish Enterprise
3.	Conchita Manabat	International Association of Financial Executives Institutes
4.	David Correia	Office of the Superintendent of Financial Institutions
5.	Isabelle Grauer-Gaynor	European Securities and Markets Authority
6.	Dr Jianhua Tang	Chinese Institute of CPAs
7.	Monica Foerster	Confidor
8.	Nana Li	Impax Asset Management
9.	Natasha Landell-Mills	Sarasin & Partners
10.	Nikolaos Papadimos	Hellenic Accounting and Auditing Standards Oversight Board
11.	Susan Coffey	Association of International Certified Professional Accountants
12.	Josephine Jackson (Observer)	IAASB Vice Chair