

# CRUNCH TIME FOR GLOBAL ADVISERS?



The top 25 networks and associations continue to show strong revenue growth – but can this be sustained much longer? **Liz Fisher** reports

**T**his year's survey of the top 25 networks and associations shows continuing strong growth in global accountancy and advisory services revenue. Many of the networks and associations show particularly impressive revenues from their work in the emerging economies. But as developed economies across the world slow, and the international credit crisis continues, there must be concerns that the current growth rates cannot be sustained for much longer.

Among the Big Four, KPMG reported an increase of 17.4% in its global revenues. Advisory services grew by 22.2% across the network, while strong merger and acquisition activity in the Asia Pacific region saw its revenues increase by almost 22%. In common with many networks, KPMG reported strong growth in the BRIC countries (Brazil, Russia, India and China), reporting aggregate revenue increases of 41% during the year.

At Ernst & Young, global transaction advisory services showed the strongest growth with 29%, which, said the firm, 'reflected E&Y's involvement in some of the largest deals over the period, including significant activity in the emerging markets, and the exceptional demand from private equity'. It remains to be seen whether E&Y and the other large networks and firms will be able to sustain revenue growth in this area in the wake of the credit crunch.

Grant Thornton International's 2008 transparency report showed a global revenue increase of 25%, the highest growth rate reported in the top six networks. Its US member firm has been the fastest-growing in organic terms over the year, reporting a 16% increase in revenues to \$1.1bn (£600m). The network also reported strong organic growth in member firms in Brazil (65%) and India (74%).

In the mid-table, Nexia International has reported growth of over 50% to take it close to Baker Tilly International, thanks mainly to its merger with SC

International in December 2007. Gareth Pearce, chairman of Nexia International, said at the time that SCI's depth in key geographical areas – the network was particularly strong in the US and Canada, Germany, South Africa and Mexico – made it a 'strong fit' for Nexia.

Horwath International also reported strong growth and has steadily added new firms and small networks to its stable during the year, including 12 firms in France and WHK Group in Australia. Elsewhere, the largest audit firm outside of the Big Four in China, Zhongrui Yuehua CPAs, signed up to RSM International. The firm has 19 offices across the country, 2,600 partners and staff, and annual revenues of over \$70m.

## To network or not to network?

Once again, it is the legal structure of the international networks and associations that is the major talking point raised by this year's survey.

The EU Statutory Audit Directive (which comes into force in the UK this summer) set out a new definition of a 'network', and this has been supported by subsequent amendments to the International Federation of Accountants (IFAC) Code of Ethics (see box on next page). Even so, there is growing acceptance that the generic use of 'network' to describe internationally operating accountancy firms is no longer appropriate because of the shifting regulatory landscape and the way the profession is adapting its practices.

The recent European Federation of Accountants (FEE) study *Trans-national Organisations and Practices within the Accountancy Profession* identified the emergence of three distinct structural models adopted by international accountancy organisations: international associations of independent firms coordinated by a separate legal entity; integrated international partnerships; and national practices with subsidiaries in other jurisdictions

## International networks and associations

International network / association	UK affiliate	Fee income \$m	Previous year \$m	Member firms	Offices	Countries	Partners	Prof staff	Year end
<b>PricewaterhouseCoopers</b>	PricewaterhouseCoopers	25,150	21,986		766	150	8,578	108,926	Jun-07
<b>Deloitte</b>	Deloitte	23,100	20,000	69	670+	142	8,500	112,000	May-07
<b>Ernst &amp; Young</b>	Ernst & Young	21,104	18,359		700+	140	7,604	89,680	Jun-07
<b>KPMG International</b>	KPMG	19,810	16,880		696	145	7,160	92,924	Sep-07
<b>BDO International</b>	BDO Stoy Hayward	4,704	3,911	100	626	110	2,520	23,729	Sep-07
<b>Grant Thornton International<sup>1</sup></b>	Grant Thornton UK	3,461	2,772	93	490	100+	2,448	18,000+	Sep-07
<b>Geneva Group International<sup>2</sup></b>	Citroen Wells, Lawrence Grant	3,146	2,491	248	351	66	1,470	12,023	Dec-07
<b>RSM International</b>	RSM Bentley Jennison	3,060	2,700	66	662	64	2,411	17,013	Sep-07
<b>Praxity</b>	Hazlewoods, Lovewell Blake, Mazars, Menzies, Forrester Boyd and others	2,840	2,400	101	348	73	2,135	23,528	Dec-07
<b>Horwath International Association</b>	Horwath Clark Whitehill	2,527	2,188	137	465	96	2,454	12,847	Dec-07
<b>Baker Tilly International</b>	Baker Tilly	2,500	2,300	138	505	104	2,629	16,336	Jun-07
<b>Nexia International</b>	Smith & Williamson, Saffery Champness, Scrutton Bland	2,300	1,497	170	620	97	2,195	17,872	Oct-07
<b>Moore Stephens International</b>	Moore Stephens	1,880	1,544	358	621	95	2,069	13,593	Dec-07
<b>HLB International</b>	Vantis, HLB Vantis Audit	1,729	1,516	150+	440+	100+	1,753	10,187	Nov-07
<b>PKF International</b>	PKF	1,723	1,480	200	257	120	1,882	10,670	Jun-07
<b>Leading Edge Alliance</b>	Streets, HW Fisher and others	1,713	1,330	144	390	82	1,200	9,400	Dec-07
<b>Kreston International Ltd</b>	Reeves + Neylan, James Cowper, Bishop Fleming and others	1,700	1,341	220	665	92	1,167	14,183	Oct-07
<b>Fiducial</b>	None	1,350	1,340	1,800+	n/a	77	n/a	14,000	Sep-07
<b>AGN International Ltd<sup>3</sup></b>	Shipleys, Dixon Wilson	1,317	1,200	200+	492	89	1,165	6,998	Dec-07
<b>MSI Global Alliance<sup>4</sup></b>	Haysmacintyre, Armstrong Watson	1,085	1,020	249	160	96	1,960	7,010	Apr-08
<b>IGAF Worldwide<sup>5</sup></b>	Buzzacott, Cooper Parry and others	1,029	915	124	350	57	945	5,853	May-07
<b>BKR International</b>	Cassons, Blick Rothenberg	894	709	135	300	70	1,013	7,090	Nov-07
<b>DFK International</b>	Chantrey Vellacott DFK	878	717	194	332	81	1,063	5,299	Sep-07
<b>IAPA</b>	FW Stephens, Wilkins Kennedy, Bird Luckin, Target Chartered Accountants and others	841	848	225	339	51	1,374	4,071	n/a
<b>Morison International<sup>6</sup></b>	Tenon Group	806	718	166	261	68	663	5,562	Dec-07

### How the table is compiled

Figures are collected from annual reviews and reports, network websites and direct from the firms themselves. Each year it becomes more difficult to distinguish between networks and associations offering 'pure' accountancy services and the more multidisciplinary organisations. As in previous years, we have included a number of multidisciplinary practices in the survey, as it is often impossible to strip out revenue earned by law practices from the overall figures. At least three networks within the top 25 – Geneva Group International, MSI and Morison International – are multidisciplinary in the sense that they have member firms that exclusively practise law. Other networks that are not strictly multidisciplinary, however, also offer services, such as stockbroking and financial advice, that are arguably outside the 'traditional' view of accountancy services.

(see p116 for a detailed discussion of the FEE study and its implications). Within these broad groups, however, the organisational approach can differ dramatically.

### Notes to table

1. Income from 15 correspondent firms excluded
2. Multidisciplinary
3. Association
4. Multidisciplinary
5. Association
6. Multidisciplinary

The firms remain divided on the question of whether a strong and cohesive international structure is the best approach, or whether international links with other firms should remain more distant and flexible.

In general, it is the larger firms that are taking steps to strengthen their global structure. E&Y recently announced that it is to integrate its practices in Europe, the Middle East, India and Africa (see p64), saying the decision reflected the 'profound changes' to the broader business environment. Grant Thornton International, meanwhile, launched a new logo and brand in February. David McDonnell, GTI's chief executive, said the new brand would support the network's strategy of becoming 'a more cohesive global organisation. The new brand is another important step in differentiating Grant Thornton in the marketplace'.

### Web addresses

www.pwcglobal.com  
 www.deloitte.com  
 www.ey.com  
 www.kpmg.com  
 www.bdointernational.com  
 www.gti.org  
 www.ggi.com  
 www.rsmi.com  
 www.praxity.com  
 www.horwath.com  
 www.bakertillyinternational.com  
 www.nexia.com  
 www.moorestephens.com  
 www.hlbi.com  
 www.pkf.com  
 www.leadingedgealliance.com  
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## Forum of Firms

One of the most significant developments during the year has been the increased profile of IFAC's Forum of Firms. The forum was established in 2002, and in January this year it announced that 17 international networks had met the requirements for full member status, with a further four networks gaining provisional status.

The Forum of Firms requires that members have, or are interested in accepting, trans-national audit appointments. Its members must agree to 'promote the consistent application of high-quality audit practices worldwide, including ISAs (International Standards on Auditing), and support convergence of national audit standards with ISAs'. Members are also required to have policies that conform to the IFAC Code of Ethics.

In one respect, though, the establishment of the

forum has only served to increase the confusion over the distinction between an international network and an association, and what that means in practice. Part of the confusion comes down to the fact that it is possible for an organisation that calls itself an 'association' to still meet the definition of a 'network' under the IFAC Code of Ethics. As a general rule of thumb, the code effectively says that if it looks like a network, feels like a network and quacks like a network, it is a network.

However, the firms that have not elected to join the forum – and these tend to be the multidisciplinary associations and those with mid-tier members who are aiming firmly at the entrepreneurial small and medium-sized enterprise (SME) market – are concerned that their organisations will somehow be perceived as being inferior. This is not helped by the forum's stated aim of improving the standards of international auditing and financial reporting.

MSI Global Alliance is among the associations that have not elected to join the forum, and its chief executive, James Mendelsohn, has argued that a looser relationship between firms in an association such as MSI can provide a more appropriate service for entrepreneurial and owner-managed businesses. Meeting the requirements of the forum, he and others argue, creates an extra bureaucratic layer and regulatory costs that could be passed down to clients who have no real need of the services a network offers.

While being part of an international network undoubtedly brings benefits, the risks involved, diminished in the memory since the Parmalat case, have been raised again recently in the US. In March, a Florida appeals court overturned an earlier ruling that had excluded BDO International from a claim against its US member firm.

The case involved a fraud uncovered in a Portuguese bank, Banco Espirito Santo, in 2002 and for which the US firm was found negligent in its audits and ordered to pay \$520m in damages. The bank had originally filed a claim against both BDO Seidman and BDO International, but the network had been dismissed from the claim in 2007 by the judge in a lower court on the grounds that the plaintiffs had not shown an agency relationship between the firm and network. The appeal court ruled, however, that the jury in that case should have been asked to decide whether BDO International should also have been considered liable. BDO Seidman's appeal is ongoing.

*Empire building, p64; Fit for purpose? p116*

## What is a network?

The EU Statutory Audit Directive introduced a formal definition of a network for the first time. According to the directive, a network means a larger structure that is:

- aimed at cooperation, and to which a statutory auditor or an audit firm belongs; and
- 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.

The IFAC Code of Ethics s290 (Revised), which applies for annual reports dates on or after 31 December 2008, builds on this definition.

The code says that the judgment of whether a firm belongs to an international network should be made 'in light of whether a reasonable and informed third party would be likely to conclude that a network exists'. In broad terms, a firm would be classified as belonging to an international network if it were part of a structure of cooperation that involves profit or significant cost-sharing, or there was common ownership, management or control. The reference to the judgment of a third party, though, means the definition is not precise. The points IFAC makes in the section include:

- If the purpose of an association of firms is only to refer work between its members, it is not a network
- If there is profit- or cost-sharing between firms, it is a network, but if the firms only share immaterial costs, for example the cost of training manuals, it is not a network
- If the firms share quality control systems and procedures, it is a network
- If the firms share a common business strategy, it is a network

The code also says that use of a common brand name is likely to indicate a network, but adds that firms should be careful about the use of brands if they do not consider themselves to be part of a network. 'Even though a firm does not belong to a network and does not use a common brand name as part of its firm name, it may give the appearance that it belongs to a network if it makes reference in its stationery or promotional materials to being a member of an association of firms,' says the code. 'Accordingly, a firm should carefully consider how it describes any such memberships in order to avoid the perception that it belongs to a network.'