

The race is on, but the field is limited in the auditin...

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Prof Prem Sikka wrote the [following article on The Conversation web site](#). I reproduce it, with permission:

Isn't it interesting how governments go through the rituals of promoting competition, but little actually changes? The latest example is the UK [Competition Commission's report](#) on the UK auditing industry.

The report is supposedly concerned with enhancing competition in the UK auditing market. The current position is dire. Thanks to the close alignment between corporate interests, policymakers and politicians, successive governments permitted restrained mergers.

Today the auditing market is dominated by just four accounting firms. These are PricewaterhouseCoopers, Ernst & Young, Deloitte & Touche and KPMG (known as the Big Four firms), and between them they audit 99 of the UK's biggest listed companies (FTSE100) and around 240 of the next 250. On average, a FTSE100 auditor remains in office for about 48 years; for the FTSE250 the average is 36 years. The Big Four firms are dominant in most western countries. Their global income from auditing and consultancy services is about £77 billion (US\$115 billion) and some £7.9 billion (\$11.9bn) of it comes [from the UK](#). This provides plenty of financial and political resources to thwart any unwelcome policies.

The probability of another accounting firm breaking into this magic circle is extremely low as the entry costs are high. The challengers need help but there is little on the table from the Competition Commission. The Commission does not want to break-up the Big Four firms or place any limits on the proportion of market they can dominate. It does not want to place any time limits on the audit firm's tenure either.

This monopoly of company audits has been the springboard for the growth of the Big Four accounting firms. Audits give accounting firms easy access to company boards and lets the accountants sell all kind of additional services, ranging from tax avoidance, advice on mergers and takeovers to printing T-shirts, badges and laying golf courses.

All this increases fee dependency on clients and must lessen the probability of speaking out against unsavoury practices. At the dawn of the banking crash, concerned savers were forming [queues](#) outside distressed banks and governments were bailing out banks, but auditors gave their customary [clean bill of health](#) to all distressed banks. This silence was not followed by any investigation by the UK government. There is no action by any regulator either. Even if they act, it takes years. The matters relating to the audit of automaker MG Rover by Deloitte were referred to the Financial Reporting Council, the UK regulator, in 2005. It [finally reported](#) on 29 July 2013.

The regulatory inertia neither encourages competition nor improves the quality of audits. Last year, a tax tribunal heard a case relating to a tax avoidance scheme designed by Ernst & Young for [liffe News and Media](#). The company was very profitable, but was concerned that healthy profits would encourage employees to demand higher wages. So Ernst & Young, who were also the company's auditors, designed a scheme that would artificially depress profits and avoid tax too. The company's board minutes stated that Ernst & Young confirmed that the use of the scheme would also "significantly lessen the transparency of reported results". Despite such episodes, the Competition Commission does not want to ban the sale of consultancy by auditors to their audit clients. The best that it can come-up with is that companies might put audits out of tender every five years.

The Competition Commission could have increased the market pressures on auditors to improve quality of audits by empowering consumers of audit opinions, but it does not do that. Auditors only owe a "duty of care" to the company rather than to any individual shareholder, creditor or any other stakeholder. So individuals can do little to bring negligent auditors to book. Court cases such as [MAN Nutzfahrzeuge AG & Anor v Freightliner Ltd & Anor \[2007\]](#) show that there is little recourse against auditors even when they are found to be negligent.

At annual general meetings (AGMs) shareholders are asked to vote on auditor appointment and remuneration, but this resolution is not supported by any information about quality of audit work, lawsuits or regulatory action against auditors. Shareholders are not given any sight of auditor working papers. Shareholders have no idea of the work done by auditors. Auditing firms are commercial concerns and their success is measured by profits. In pursuit of profits, the firms reduce the time allocated to each audit even though audits are labour intensive and need a higher time budget. The hope is that aspiring accountants will work evenings and week-ends for free. Academic research shows that a large number of audit staff do not go along with such strategies and resort to [falsification of audit work](#) or ignore awkward transactions because they require more time than is allocated. Audit failures are manufactured by the business model and organisation culture of accountancy firms, but this does not even appear on the radar of the Competition Commission.

There is little meaningful public information about auditors. There is no public availability of audit contract, information composition of the audit team, time spent on

the job, details of meetings with company directors, or anything else that might enable the consumers of audit opinions to assess audit quality.

The Competition Commission has capitulated to the [lobbying power](#) of the Big Four and failed to introduce any meaningful reforms. Maybe such issues will be considered after the next banking crash.