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Liberalising audit markets for local government: The five forces at work in England and the Netherlands

Dennis de Widt, Iolo Llewelyn, Tim Thorogood

Abstract

Both England and the Netherlands have seen efforts to liberalise their audit markets for local government in recent decades. According to economic theory these should benefit buyers as increased competition produces lower prices and improved quality. Increasing the number of competing audit firms in markets traditionally dominated by few, large, firms is widely seen as a key ingredient to this process. However, liberalisation has taken different paths in England compared to the Netherlands. In England, a national level collaborative purchasing arrangement has seen a small number of large firms competing whilst in the Netherlands a free market has led to withdrawal by Big-4 firms and rapidly growing market share by mid-tier and small firms. In this paper, we analyse contrasting market developments in local public audit in England and the Netherlands and accordingly analyse the underlying factors through applying an established framework for market analysis from industrial economics, Porter's five forces framework, together with an institutional logics approach to further understand the factors involved. We find the Porter framework a useful tool to identify structural differences between markets but one that requires further analysis to explain underlying dynamics which in the case of Dutch and English local public audit markets is effectively provided by use of concepts from institutional logics including a historical contingency analysis.

Keywords: England, five forces framework, institutional logics, local government auditing, the Netherlands, Public Sector Audit Appointments Ltd

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1. INTRODUCTION

Audit market concentration excites the interest of policy makers and academics alike concerned that concentration reduces competitiveness and quality whilst encouraging higher fees. There are few studies however of how markets have evolved, and available studies provide conflicting evidence on the relevance of critical factors such as economies of scale or client preference for larger firms (Van Raak, Meuwissen, & Schelleman, 2019) whilst also suggesting that different markets and segments behave differently (Carson, Redmayne, & Liao, 2014; Gunn, Kawada, & Michas, 2019; Simunic, 1980). Understanding market evolution is critical to ensuring that steps taken to improve competition will actually be effective. Cross country comparisons which enable factors underpinning contrasting markets to be identified are particularly valuable, but they remain rare (e.g., Francis, Michas, & Seavey, 2013; Gunn et al., 2019). Equally rare are studies of public sector markets generally and local public body markets in particular despite their large size and evidence of their different structures (Clatworthy, Mellett, & Peel, 2002). This article aims to address these gaps by undertaking a cross country comparison of local government (LG) audit market development. We compare the development of LG audit markets in England and the Netherlands which have both seen substantial steps towards liberalisation as public sector sponsored dominant purchasers and providers were replaced by free markets where individual LGs could each appoint their own auditors. In England, a single state purchaser which had also dominated the supply market with its own ‘in-house’ audit arm was ended after 2010 and in the Netherlands a firm owned by the municipalities which had dominated the market became independent in 1987 and then merged with Deloitte and Touche.

Economic theory would suggest that these developments should improve competition by enabling smaller and/or new firms to develop in the market and as a result improve quality and prices. However, liberalisation has taken different paths in England compared to the Netherlands. In England, a national level collaborative purchasing arrangement has seen a small number of firms competing whilst in the Netherlands a free market has led to withdrawal by Big-4 firms and rapidly growing market share by mid-tier and small firms.¹ By comparing England and the Netherlands we therefore take two countries, with relatively similar policy objectives and procurement law, both liberalising LG audit markets which have taken different

¹ The Big-4 firms are Deloitte, EY, KPMG, and PwC. There is no definition of mid-tier and small firms – for the purpose of this paper, we define mid-tier firms in England as all firms with a turnover exceeding 50million pound but excluding the Big-4 (14 firms in 2019), whilst small firms include all accountancy firms with a turnover of less than 50million pound. For the Netherlands, we use a similar definition and define mid-tier firms as all firms, excluding the Big-4, with a turnover exceeding 50million euro (12 firms in 2019), whilst small firms include all accountancy firms with a turnover of less than 50million euro.

paths with outcomes which show important similarities and differences. Our key research question is: *why have two relatively similar countries with liberalised markets for local government audit achieved different outcomes in terms of market composition?*

To facilitate structured comparison and link with economic theory we initially use a widely recognised framework from industrial organisation analysis, the five forces framework of Michael Porter (Porter, 2008) before then applying concepts from institutional logics to analyse the identified differences. We identify that ‘entry barriers’ (the first of the five forces) are higher in England due to several factors. We also find that a further force, ‘buyer power’, contrasts significantly as the purchasing consortium in England procures audit contracts for large, national lots which prevents smaller firms from competing whereas medium or small firms in the Netherlands could easily compete for single contracts at individual LGs. However, analysis of a further force, ‘competitive rivalry’ between firms, shows that in England the purchasing consortium approach had been able to retain the interest of larger firms in the market, whereas in the Netherlands a system of municipal level audit appointments has led to larger firms vacating the market thus creating opportunities for smaller firms.

The existence and approach of the English purchasing consortium thus emerges as a critical factor in explaining the differences in audit market evolution, mediated through different entry barriers, buyer power and competitive rivalries. We therefore consider why Dutch LGs have not developed a national purchasing consortium as in England, given its obvious benefit in retaining large firm interest. Here the institutional logics concept of field level blending is used to show why England developed a new form of LG audit appointments whilst the Netherlands largely continued with the existing approach. The research for this paper draws on a variety of empirical sources, in particular semi-structured interviews and documentary analysis, whilst for the Dutch case a statistical analysis has been conducted too.

This paper is structured as follows. We first review the relevant literature, followed by the introduction of our theoretical framework. We then summarise the main institutional developments and LG audit market features in both countries over the periods when they underwent market liberalisation before setting out our methodology. Drawing on our theoretical framework, we then analyse each countries’ current audit markets. The paper concludes with a summary of findings, theoretical implications, and suggestions for further research.

2. LITERATURE REVIEW

Audit market concentration is a much-studied topic. Explanations have focused on the size advantages of larger audit firms; in terms of quality (DeAngelo, 1981), cost (Danos & Eichenseher, 1986), or capacity (Doogar & Easley, 1998). Overall views that market concentration results from a lack of competition and leads to cost and quality problems are contrasted with views that concentration has arisen as a natural response to client firms' demand for audit quality and that cost and quality are conditional on client demands and audit complexity (Van Raak et al., 2019). Audit concentration has also been considered by many official sources. A 2011 UK House of Lords report identifies multiple causes for concentration including the internationalisation of business, capital requirements, economies of scale, a perception that big firms deliver better quality, and the reputational assurance of using Big-4 auditors (House of Lords, 2011, p.10)

One of the most discussed but inconclusive issues is whether market concentration of itself reduces competition. The traditional Structure Conduct Performance paradigm of industrial economics holds that market structure affects firms, resulting in abnormally high profits where markets are concentrated (Lipczynski, Wilson, & Goddard, 2005). However, the validity and empirical support for this logic has been questioned by new industrial organisation theories and specifically for audit markets (Ballas & Fafaliou, 2008; Beattie, Goodacre, & Fearnley, 2003). Even if concentration of itself does not reduce competition it can provide barriers to entry to new firms amongst larger client segments due to factors such as perception bias against mid-tier and smaller audit firms, the high costs of entry, a long payback period for investment and significant business risks (Oxera, 2006).

Whatever the causes and effects, many audit markets are unarguably highly concentrated. Under the definitions of new industrial economics, where four firms have over 60% of the market it is classified as a 'tight oligopoly' (Ballas & Fafaliou, 2008; Oxera, 2006). Across the EU, the audit market concentration ratio (CR4) increased from 63% in 1998 to 73.7% in 2004 (Ballas & Fafaliou, 2008).

Although they are concentrated overall, audit markets are simultaneously segmented. Simunic (1980) proposed that audit markets consist of an oligopolistic segment of large audit clients and a competitive segment of small audit clients. The 'size effect' whereby larger clients prefer large audit firms has been much discussed (e.g., Beattie et al., 2003; Lowensohn, Johnson, Elder, & Davies, 2007) but attention has also been given to how, in a 'differentiated oligopoly' specialisation is a source of competitive advantage by firms (Numen & Willekins, 2011). The complexity of audit markets which can exist underneath the 'headline figures' of Big-4 dominance is detailed in Carson et al.'s (2014) analysis of Australian audit which finds

that concentration and competitiveness differ according to company size, with the large audit firms maintaining over 90% of the largest clients but mid-tier accounting firms growing market share in the medium and small client markets, indicating a competitive but segmented market.

A small but growing literature investigates audit markets in the public sector (Ferry & Ahrens, 2021; Hay & Cordery, 2018). Some of these studies are primarily concerned with whether the principle of marketisation should be applied to public audit, such as English's (2003) review of the marketisation of Western Australia's state auditing which finds the concept of the private sector auditing state institutions misconceived due to fundamental differences of accountability and scope. Other studies apply a broader perspective and analyse how the management of public services is affected by changes to accountability frameworks (e.g., for the UK, see Murphy, Ferry, Glennon, & Greenhalgh, 2019).

Amongst the studies investigating the development of public audit markets, a small number analyses local public audit markets (LGs and other local bodies such as hospitals, fire and police services). A study by Lowensohn et al. (2007) of the Florida LG audit market shows how the market share of large audit firms substantially decreased in the period 1993-2003 after procurement regulations were liberalised and suggests that reduced market interest and client selectivity by large firms created opportunities for smaller firms. Big-4 dominance of local public audit markets is also reported in Tagesson, Glinatsi, and Prah (2015) study of the Swedish LG audit market where Big-4 companies won all the 189 municipal audit contracts included in the study, with audit contracts mainly awarded on the basis of price. Comparing NHS trust audits in England with those in the private sector, Clatworthy et al. (2002) find that large audit firms do not charge a premium for their audit services in the NHS, which they suggest might be due to a preference amongst large firms to participate in this market to maintain their public sector profile rather than maximise profitability. The authors conclude that structural differences exist between the two sectors and called for further research to ascertain how far generalisations can be applied to different markets including LG markets.

In this study, therefore, we seek to deepen our understanding of audit market development through examining two contrasting LG audit markets on a country comparative basis – England and the Netherlands. Identifying causal factors on a cross country basis requires a consistent macrolevel analytical framework which is introduced in the next section.

3. THEORETICAL LENS

In new industrial organisation theories, the five forces model by Porter (2008) provides a consistent framework for assessing and comparing the competitiveness of different markets

through identifying which underlying ‘forces’ are most salient in terms of structure and supplier/client behaviour (e.g., Lipczynski et al., 2005). For public sector markets it has been used to understand competition in higher education (e.g., Mahat, 2018) but to our knowledge not for the analysis of local public audit markets.

According to Porter’s model, an industry’s structure is determined by five factors, depicted in Figure 1, which interact to determine market attractiveness and competitiveness. Analysis using the model should identify which forces are salient in a given market as well as their causal dynamics. We discuss these forces, including their potential relevance to local public audit.

- *Insert Figure 1* -

Threat of entry assesses how difficult it is to enter a market due to entry barriers such as economies of scale (including ‘demand side’ economies of scale where buyers prefer firms with a large market share), other incumbency advantages (e.g., brand, experience, location) or regulatory policies. In audit markets, entry barriers, which include regulatory barriers are widely seen as significant, in addition to competitive barriers albeit recent evidence questions whether in fact they deter new entrants (Kitto, Lamoreaux, & Williams, 2020).

Power of suppliers is a factor whereby entities controlling essential resources for an industry (such as labour) are able to control and restrict supplies to firms competing in the market. In the case of the audit market, we see licensing organisations as constituting suppliers as they effectively control the supply of licensed auditors and audit firms.

Buyers are powerful if there are few of them and/or they purchase in large volumes relative to vendors, where the products are standardised and/or switching costs are low and/or where they can credibly threaten to integrate backwards. Buyers will be price sensitive under certain conditions including where they are strapped for cash, and/or where quality or cost of buyers’ services are little affected by the vendors’ services.

Substitutes offer the same result but by different means. If there is a real possibility of substitution, then an industry is less attractive. In the case of LG audit, it may be hard to see substitution by a different service unless the regulatory regimes change, but substitutes could also include changes to how audits are resourced through new technology or new methods, for example, which could threaten the position of incumbents.

The fifth factor is rivalry among existing competitors within the industry: where this is intense then profitability suffers, and the industry is unattractive. Rivalry is affected both by

the intensity with which firms compete and by the basis on which they compete. Intensity is greater where competing firms are numerous or equal in size and power, where growth is slow, exit barriers are high, and firms are highly committed to the industry, or where firms have diverse approaches to competing which create on-going new pressures. The basis on which firms compete refers to whether firms compete on the same dimension e.g., price or different dimensions (e.g., service features). Where firms compete on the same dimension then rivalry will be more intense, particularly where this dimension is price since prices are usually transparent and easy to imitate.

The studies discussed above indicate the importance of the intensity of competitive rivalry as a factor in audit markets but also highlight how it remains uncertain, for example how far rivalry exists within the larger client/large firm segments or the importance of price compared to brand (Carson et al., 2014; Numen & Willekins, 2011; Van Raak et al., 2019). The existence of additional forces is often discussed with various suggested candidates including government generally (e.g., McGinn, 2010) and regulation specifically (Mahat, 2018) albeit Porter himself argued otherwise (McGinn, 2010). Due to our findings we return to this debate in our conclusion.

The five forces framework helps to clarify the structural differences in LG audit markets and why there might be consolidation in some but fragmentation in others. However, it leaves open the question as to why these structural differences developed in terms of actor responses to changing institutional environments, and it is here we make use of institutional logics (Friedland & Alford, 1991; Thornton, Ocasio, & Lounsbury, 2012). The institutional logics approach connects organisational form, normative frames of reference and individual agency within substantial social theory. Major social forms such as market, state, community and profession provide ‘logics’ – ‘socially constructed, historical patterns of cultural symbols and material practices, assumptions, values and beliefs by which individuals produce and reproduce their material subsistence, organise time and space, and provide meaning to the daily activity’ (Thornton et al., 2012, p. 12) - which then provide normative frames of reference that guides individual actors in organisations.

A key meta-theoretical assumption of the institutional logics approach is historical contingency which focuses attention on how the effects of economic, political, structural, and normative forces affecting individuals and organisations might be historically contingent. Organisational fields are characterised by distinct institutional logics that are relatively stable and change only over long periods of time (Friedland & Alford, 1991, p. 132). Drawing on prior knowledge and experience in relation to the prevailing institutional logics, however,

individuals and organisations have the capacity to recognise and attend to institutional logics and apply them strategically. Hence, given that a plurality of logics influences actors in organisations, how organisations develop will reflect accommodations between actors and their logics.

Against the backdrop of societal level logics, logics also develop at field (industry) level. Linked to the overall logics of the interinstitutional system, these generate distinct forms of instantiation, variation, and combination of societal logics and typically coexist in multiple and even competing forms and are dynamic (Thornton et al. 2012, p. 174). According to the direction and extent of change, field level logics can become hybridised rather than one replacing another (Haveman & Rao, 2006). Skelcher and Smith, (2015) distinguish between different types of hybrids including the blended hybrid which they define as the ‘synergistic incorporation of elements of existing logics into [a] new and contextually specific logic’ (p. 440). We use the concepts of blended field level logic to assess how England developed through PSAA a blending of the previously dominant professional and bureaucratic logic with that of a market logic forced on the LG sector by central government. This contrasts with the Netherlands where no such accommodation of institutional logics was required as the dominant market logic governing LG auditor appointments continued.

4. INSTITUTIONAL AND MARKET FEATURES OF ENGLISH AND DUTCH LOCAL PUBLIC AUDIT

Local public audit in both England and the Netherlands has experienced significant transformation over recent years.

4.1 England

Pre-2010, the Audit Commission was the dominant organisation in local public audit in England. The Commission, which was established by the Local Government Finance Act 1982, fulfilled various roles, most significantly overseeing local public audit as regulator, commissioner and provider of local external audit services. On its establishment, the Commission’s responsibilities extended to LG in England and Wales; these were later extended to health service bodies, but responsibility for all audits in Wales were lost in 2005. The auditors commissioned to undertake the audits were a mix of around 70% from the Commission’s in-house audit arm, and some 30% from private sector accountancy firms (Campbell-Smith, 2008). The firms were invited to tender for a share of the 30% allocated to the private sector.

In 2010, radical changes were made to the arrangements for LG audit in England which culminated in the abolition of the Audit Commission. Table 1 summarises the allocation of audits for 2012-13 following the closure of the Commission's in-house practice. The Local Audit and Accountability Act 2014 (the 2014 Act), which provided for the Commission's abolition, allowed each LG body to appoint its own auditors, albeit with some requirements regarding the independence of the appointment process. Following successful lobbying by the English Local Government Association (LGA), the 2014 Act also included a clause that enabled the Secretary of State for Communities and Local Government to specify one or more organisations to act as Appointing Persons who could develop a collective scheme for the appointment of local auditors. In 2016, the LGA successfully submitted its own wholly owned company Public Sector Audit Appointments Limited (PSAA) to the Secretary of State as the appointing body for England's principal local authorities from 2018/19.

- *Insert Tables 1 & 2* -

Out of a total of 494 bodies eligible to join the PSAA scheme, 484, or 98%, decided to opt-in. In 2017, PSAA awarded contracts to six audit firms/consortia for a five-year appointing period, the outcome of a competitive tendering process, details of which are included in Table 2. In contrast to what was expected by PSAA, submitted bids enabled PSAA to reduce scale fees by 23% compared to the preceding year, continuing previous reductions realised by the Audit Commission of 40% in 2012 and 25% in 2015 (De Widt, Llewelyn, & Thorogood, 2020). The successful firms/consortia are listed in Table 1 and include both Big-4 and mid-tier audit firms. The size of the lots was graduated in order to reward the better tenders with larger volumes of work, with lot sizes ranging from £14.6m to £2.2m. One further lot with no guaranteed value was also let to enable a last resort option if the auditors from the five substantive lots presented independence issues (PSAA, 2018).

In 2019, the government commissioned a post implementation review of the changes introduced by the 2014 Act. The resulting report (Redmond, 2020), issued in September 2020, made various recommendations to improve the arrangements for local audit, some of which would effectively reverse some of the measures introduced by the 2014 Act, at least in part. The recommendations focused on supporting immediate market stability and improving 'system leadership' by establishing a new body, the Office of Local Audit and Regulation (OLAR), to manage, oversee and regulate local audit (Redmond, 2020). The government's response, published in May 2021, generally accepted the recommendations regarding market

stability, but rejected the establishment of OLAR. Instead, the Ministry of Housing, Communities and Local Government (MHCLG) has proposed that the Audit, Reporting and Governance Authority (ARGA), announced in 2020 as a replacement for the Financial Reporting Council (FRC), would perform the role of ‘system leader’ with ‘overarching responsibility for the local audit framework, including the Code of Audit Practice and the monitoring and review of local audit performance (MHCLG, 2021).

4.2 The Netherlands

Whilst Dutch municipalities have always appointed their own auditor, at least since a professional audit has been in place, historically the Association of Dutch Municipalities (VNG) played an important role in Dutch municipal audit. The VNG had its own audit firm, called VB Accountants, which was the preferred auditor of most Dutch municipalities. In 1987, VB Accountants became independent from the VNG, and, as it was perceived too small to compete against the large firms, it merged with Deloitte & Touche into VB Deloitte & Touche, today known as Deloitte (Breij & Brouwer, 2009). Deloitte long remained the dominant player in the Dutch municipal audit market, with the rest of the market occupied by the other large firms.

In recent years, the Dutch municipal audit market has become increasingly dynamic with Big-4 firms withdrawing from the market and smaller and midsize players entering. Whilst KPMG had left the market in the early 2010s, EY completely withdrew from the market by the end of 2019. Deloitte and PwC, as the remaining Big-4 firms, have in particular withdrawn from auditing small (<25,000 inhabitants) and midsize municipalities (<100,000 inhabitants). A survey conducted on behalf of the Dutch Interior Ministry shows that in 2014 and 2015 Deloitte, EY, and PwC, stopped auditing at least 107 Dutch municipalities (out of a total of 393), with all except one of these municipalities having a population of less than 100,000 inhabitants (BMC, 2016). Our qualitative evidence indicates that in most cases this was a result of Big-4 firms not participating in municipal tenders or being unsuccessful in those tenders due to their higher pricing. Instead, Deloitte and PwC have increasingly focused on auditing large municipalities, which is reflected by the fact that out of the 31 Dutch municipalities with a population exceeding 100,000 inhabitants, out of which 29 are being audited by a private sector firm, 27 are audited by either Deloitte or PwC (with both firms holding relatively equal market shares), whilst only two 100,000+ municipalities are audited by a non Big-4 firm.

Table 3 provides an overview of the firms active on the Dutch municipal audit market in 2013, 2016 and 2019. The table shows that whilst the Big-4 audited 89.2% of Dutch municipalities in 2013, their market share shrank to 23.7% in 2019. Although the withdrawal by Big-4 firms has caused capacity issues on the Dutch municipal audit market, most market space has been effectively occupied by mid-tier and small audit firms. Mid-tier firms have gained the largest market share on the Dutch local public audit market, occupying 42.8% of the market by 2019, whilst small firms occupied a market share in 2019 which substantially exceeded that of the Big-4 (33.0% for small firms vs. 23.7% for the Big-4). Notwithstanding their dominant market share, some mid-tier firms reduced their market share between 2016 and 2019 (Baker Tilly Berk and Mazars). Equally, as is detailed in Table 4, not all small firms who expanded their municipal client base retained those auditees over the period 2013-19.

- *Insert Tables 3 & 4* -

Combining the five forces framework with the previous audit market research to analyse the differently evolved English and Dutch LG audit markets we would expect to see that different levels of entry threat exist to explain why the Netherlands has seen numbers of mid-tier and small players emerging contrasted to England which has remained dominated by large firms. We also expect that competitive rivalry may differ between the English market dominated by a single purchaser and the Dutch market consisting of many small purchasers, consistent with audit market segmentation theories. Related to this but not previously explored in audit market research we consider that buyer power may be influential given the presence of a single purchaser for most local authorities in England, in contrast to the Netherlands where individual appointments dominate.

Before analysing the market trends in England and the Netherlands in detail, the next section outlines our methodological approach and reports on the quantitative investigation we conducted for the Dutch case.

5. METHODS

Our investigations relied predominantly on qualitative methods, encompassing semi-structured interviews and documentary analysis. Due to municipal audits in the Netherlands mainly being procured by individual municipalities, it was possible for the Dutch case to also conduct a statistical analysis of the determinants of audit firm appointment decisions by individual

municipalities. Below, we discuss our quantitative research for Dutch LGs, but start by outlining our qualitative research approach.

5.1 Qualitative methods

The two country cases, we study here, England and the Netherlands, were chosen in light of the significant shifts audit markets for LGs experienced in both countries following liberalisation, however with very different results for market composition. A cross-country analysis of diverging audit market trends facilitates identifying institutional features that are critical to explain differences in LG audit market composition, and their impact on audit quality as perceived by key stakeholders. We gathered and analysed publicly available documentation for both countries including official reports and commentaries by practitioners active in LG audit. In addition, we received unique access, provided by PSAA, to documents unavailable in the public domain such as correspondence between PSAA and audit firms, and PSAA and LGs.

The methodology used for this study also includes semi-structured interviews. Between 2018 and 2020, we conducted 68 interviews with LG officials, auditors based in accountancy firms of different sizes, and other key stakeholders including local authority representative bodies, local authorities' treasurers associations, and professional accountancy bodies. The English interviews totalled 43, whilst 15 interviews were conducted for the Dutch case. All researchers were involved in conducting the English interviews, whilst the Dutch interviews were conducted by one of the researchers.² The interviews were digitally recorded and then professionally transcribed. The subsequent analysis was conducted using theoretical thematic analysis in which we coded the data drawing on Porter's five forces framework in combination with key concepts from institutional logics to provide a prior direction for the thematic analysis. Whilst theoretical thematic analysis tends to provide a less rich description of the data overall when compared to a more inductive coding strategy, it is a more relevant strategy if one is interested in a detailed analysis of some aspect of the data resulting from a specific research question, as is the case with our focus on market composition trends (Braun & Clarke, 2006; Hayes, 1997).

The thematic analysis was conducted by the full research team and included extensive discussion of interrelationships between themes and the various findings, with a focus on cross country similarities and differences in our findings. Plausibility of findings has been pursued through presenting contextualized understandings, theoretically informed explanations

² Necessitated in part due to linguistic differences as only one of the authors speaks Dutch.

(Parker, Schmitz, & Jacobs, 2021), and the employment of a multitude of research methodologies.

5.2 Statistical analysis of Dutch municipal audit procurements

For the Dutch case, a statistical analysis was conducted to investigate how local level factors may explain why an increasing number of Dutch municipalities have appointed small or mid-tier audit firms. A similar local level analysis was impossible to conduct for England as virtually all LG audit appointments in England are not made locally but centrally, by PSAA. Whilst we recognise that the use of mixed methods might provide for a higher level of certainty regarding our findings for the Dutch case, we increased reliability of our English findings by relying on an extensive qualitative empirical base, which, in addition to a large number of expert interviews, included unique access to documents related to PSAA's run procurement and its managed allocation of auditors to English LGs. This strategy ensured we considered material most relevant for the analysis of local public audit market shifts in England.

When allocating firms to authorities, PSAA considered firm location, and tried to ensure that the allocation for each firm included a blend of authority types (PSAA, 2017a). Table 5 shows that each firm was allocated a mixture of larger audits and smaller audits. As a result of the centrally managed allocation process the average fee per audit per firm was within a fairly narrow range of £45,601 to £55,130, whereas the actual audit fees ranged from some £4,000 for a miscellaneous body to £242,000 for a large Metropolitan District Council.

- *Insert Table 5* -

In contrast to the centrally managed allocation of auditors to English LGs, local level appointment of auditors in the Netherlands enabled statistical analysis. We employed a logistic regression model specification which is appropriate given that our dependent variable is concerned with whether or not a Dutch LG appoints an auditor different from a Big-4 firm. Based on a review of the audit literature and our knowledge of the specific Dutch institutional context as observed in our qualitative research, we tested the following empirical model to identify the effect of the regressors on the dependent variable auditor appointment:

$$Y(\text{nonbig4}) = \alpha + \beta_1(\text{tenders}) + \beta_2(\text{priceratio}) + \beta_3(\text{length}) + \beta_4(\text{population}) + \beta_5(\text{debt}) + \beta_6(\text{distance}) + \varepsilon$$

The regressor *tenders* refers to the number of tender submissions received by a municipality and has been included since most interviewees expected this to be a key factor determining the size of the audit firm being appointed, with LGs receiving a higher number of tender submissions expected to appoint a Big-4 auditor more often. The variable *priceratio* is the weight allocated to price by a municipality in the evaluation of its tender submissions. The variable's inclusion is motivated by prior private and public sector studies which demonstrate that Big-4 auditors often charge an audit fee premium compared to non Big-4 auditors (Basioudis, & Ellwood, 2005; Choi, Kim, Liu, & Simunic, 2008; McMeeking, Peasnell, & Pope, 2006). Hence, LGs less focused on achieving a low audit fee – as reflected by them putting a lower weight on price during the tender evaluation process – are expected to be more likely to appoint a Big-4 auditor. Auditors we interviewed similarly mentioned the relevance of length of the audit contract, with Big-4 auditors emphasising more strongly compared to auditors from other firms the importance of minimum contract length (with a 4-years length mentioned most frequently). Hence, we include *length* as additional regressor, which refers to the length of the audit contract in number of years. In line with previous studies showing that Big-4 firms are more likely to audit large and more complex organisations (Mellett, Peel, & Karbhari, 2007), we include the variable *population* in order to analyse the impact of municipal size on the appointed audit firm. The variable *distance* refers to travel distance between the auditor's office and the municipal auditee and has been included following the suggestion by multiple interviewees that Big-4 firms have become less willing in recent years to bid for audit contracts at municipalities which are located at greater distance from the auditor's office. Finally, prior evidence on client acceptance decisions by audit firms suggests that Big-4 firms are less willing to accept clients carrying higher financial risks (Hsieh, Chan-Jane, & Hsieh, 2018; Rama & Read, 2006). To analyse the relevance of this observation within the Dutch municipal audit context, we added the variable municipal debt (measured as percentage of total municipal income), since debt is considered an important financial risk indicator for Dutch LGs (De Widt, Thorogood, & Llewelyn, 2021). In our model, *Y* is measured dichotomously, coded 1 if a municipality appointed a non Big-4 auditor, and 0 if they appointed a Big-4 auditor. Table 6 provides further detail on the sources and measurements of the variables.

- *Insert Table 6* -

The empirical data on the audit procurements were collected from the website *Tenderned.nl*, which is the main Dutch public sector procurement portal. This enabled us to obtain data on 95 municipal audit contracts procured between 2015-2020 (2015 is the earliest year from which municipal audit procurement data are available). The variable *distance* was measured by identifying (using Google Maps) the travel distance in kilometres between the municipality's townhall and the audit office of the firm responsible for conducting the audit. Except in four cases, the responsible audit office could be identified from the published contract award notices, resulting in a final dataset utilised for the analysis containing complete data on 91 municipal audit procurements. Table 7 reports the summary statistics and shows that the average audit contract length is 3.2 years whilst on average a Dutch municipality receives 2.3 tender submissions for its audit procurement.

- *Insert Table 7* -

Table 8 shows the results of the logistic regression. The variable *tenders* is highly statistically significant and negatively associated with a non Big-4 auditor appointment (coefficients $\beta = -0.484$, $p < 0.01$), indicating that, in line with expectations, an increase in the number of tender submissions received makes it more likely that a Big-4 auditor will be appointed. In line with expectations the coefficient for *priceratio* is positive and significant, indicating that as municipalities attach a higher weight to price in the evaluation of their tender submissions, they are more likely to appoint a mid-tier or small audit firm. The impact of the variables for contract length and population lack significance, which could be caused by the fact that our dataset contains observations starting from 2015 onwards, whilst interviewees indicate that increased emphasis by Big-4 firms on longer contracts and auditing of larger municipalities is from relatively recent date. The variable *debt* similarly lacks significance. The presence in the Netherlands of an explicit bailout system for financially distressed municipalities may explain why audit firms are not deterred from taking on municipal clients with a high debt-to-income ratio. Finally, distance between an audit firm's office and the municipal auditee has no significant impact on the size of the appointed audit firm, which indicates that for a majority of firms, regardless of firm size, larger travel distance does not pose a barrier for taking on a municipal auditee.

- *Insert Table 8* -

In sum, the statistical results provide additional support for some of the key qualitative findings we present in the next section, namely that number of tender submissions and the allocated weight to price in the procurement of the audit contract are important explanations for firm size of the appointed auditor, with Dutch municipalities receiving a small number of tender bids and putting more weight on price more likely to appoint a small or mid-tier audit firm. This highlights that shifts on the Dutch market of municipal audit, with an increased share occupied by mid-tier and small firms, results from a combination of both firm level decisions, leading to a reduction in tender submissions LGs receive, and municipalities' own choices whilst procuring their audit contract.

In the remainder of this paper, we draw on extensive qualitative evidence in our analysis of market trends in both systems, applying our theoretical framework on a comparative basis.

6. FIVE FORCES INDUSTRY STRUCTURE ANALYSIS

6.1 The power of suppliers

Registration requirements for audit firms are in place in both countries. In England, a special registration applies for audit firms undertaking LG audit, who need to register with a Recognised Supervisory Body (RSB), which is the Institute of Chartered Accountants in England and Wales (ICAEW). At the date of the PSAA tender, only ten firms had registered as LG auditor, of which only one was a small firm.³ Registration requirements include the need for 'key audit partners' (KAPs) to act as engagement leads for local audits, which encompasses both LG and health audits.

The KAPs must meet detailed eligibility requirements set by the Local Audit and Accountability Act 2014 and the FRC (2019), including the requirement to hold an audit qualification for local audit, demonstrate at least two years of local audit experience, whilst the audit firm must undertake that it will satisfy itself that the KAP has adequate knowledge of the regulatory and reporting requirements relevant to local public audit. Across the UK there are only 103 audit partners who are authorised to act as KAPs in local public audit (Redmond, 2020, p. 19). To participate in the LG audit market, unregistered firms would need to recruit/develop KAPs, whilst registered firms not currently undertaking LG audits need to ensure they continue to have suitably experienced staff. These features illuminate the prominence of a professional logic in England with regard to local public audit work, a logic

³ The current number of registered firms is 9.

which was defended by multiple stakeholders we interviewed (e.g., CIPFA), although some interviewees criticised the logic as they considered LG audit ‘no more specialised than any other industrial sector’ (ICAEW) (cf. De Widt et al., 2020, p.18).

Research undertaken on unregistered firms indicate that there was a lack of awareness of the local audit environment and the possible barriers to entry. Among those firms we interviewed who were aware of the registrations some considered that the registration requirements did constitute a deterrent to entry into the market. Other firms considered that the registration requirements did not create a ‘particular barrier’ or at least it was a barrier that ‘can be overcome’. Unregistered firms currently have only limited capacity to undertake local audits, particularly lacking skilled staff (Touchstone Renard, 2020). Firms therefore recognised that overcoming the barrier created by the need to register was dependent on recruiting suitably experienced staff.

However, recruiting suitable staff was recognised to be challenging. This challenge had two dimensions: firstly, finding suitably experienced staff, possibly through approaching former Audit Commission staff who were still working as contractors. The second challenge was described as a potential ‘chicken and egg’ conundrum by one unregistered auditor: do firms invest in additional staff prior to tendering to facilitate a credible bid or wait until winning a contract before undertaking the recruitment. While the first option would be most likely to assist a firm in submitting a successful tender, failing to win a contract would leave a firm with surplus staff.

Contrasting to England, there are no specific national registration requirements for auditors undertaking LG audit in the Netherlands, except the standard registration requirements applying to all accountants to register with the Dutch professional body for accountants, and for accountants undertaking statutory audits to register with the Netherlands Authority for the Financial Markets (AFM). Whilst tendering their audit contracts however many Dutch municipalities include additional requirements in relation to the compulsory auditor registration such as the requirement for auditors to demonstrate sufficient experience in municipal audit, often by providing references from previous audit engagements. Hence even though statutory legislation is absent that requires Dutch auditors to have a specific qualification or experience in local public audit, in practice most Dutch LGs include experience as a key requirement in their audit procurement.

Consequently, and similar to England, actors in Dutch local public audit reflect a professional logic, with municipal audit perceived a specialised activity requiring substantial sector experience. Several of our interviewees traced the roots of this logic back to the days in

which VB Accountants audited most Dutch LGs, whilst those who were not mostly relied on a municipal based audit service. Both types of audit services, including the predecessor of VB Accountants, which is the Verification Bureau (*Verificatiebureau*) founded in 1914, were uniquely focused on auditing subnational public bodies, and interviewees stated that the ‘deep knowledge and understanding of the sector’ possessed by auditors at these bodies, contributed to a perception held by most municipalities that municipal audit required a specialised auditor, even though a small number of municipalities deliberately opted for auditors primarily based in the private sector, often those LGs eager to learn from private sector financial management practices.

Despite VB Accountants no longer existing as a separate organisation, many of its former staff continued to work in municipal audit, often as part of the specialised subnational audit division of Deloitte, with which VB Accountants merged, but some employed by other firms, or starting their own firm. The continuation, also after the abolition of VB Accountants, of a specific segment of auditors focused on municipal audit contributed to the sustainment of the professional logic, which is reflected by the experience requirement included in most Dutch municipal audit procurements and the obligation of a firm active in municipal audit to have a representative in the NBA’s Sector Committee on Subnational Government. The NBA’s Sector Committee aims to discuss and coordinate regulatory and other developments affecting work of auditors active in subnational government. Although we found different views as to the Committee’s effectiveness, the knowledge sharing occurring within this group was perceived by most interviewees as helpful particularly for new entrants to municipal audit.

The experience criterion was perceived by most interviewees as making local public audit significantly less attractive to new entrants as the necessity to develop local audit expertise was perceived costly. To alleviate capacity issues, the Dutch Interior Ministry has suggested municipalities should remove the experience criterion from their audit tenders (BZK, 2017). This suggestion however has only been taken over by a small number of municipalities, some of which later regretted having made this move as their appointment of a firm inexperienced with local audit was less than satisfactory.

As larger municipalities often require tendering firms to be able to submit references from previous audit engagements at municipalities of comparable size, moving up the ladder from auditing small and midsize municipalities to large ones – generally those considered above 80,000 inhabitants – was perceived by interviewees as posing a considerable barrier for small and mid-tier firms. This difficulty is exacerbated by the fact that larger municipalities in particular appear hesitant to move to a non Big-4 audit firm, which partly results from the

municipal perception that once having switched to a smaller firm it would be challenging to move back to a Big-4 auditor. An interviewed Big-4 auditor indicates that these views are not ungrounded:

We are a bit reluctant to take on clients who have previously been audited by a small firm, because we could end up with a lot of error correction work, [-] which itself is a difficult procedure and may force us to go to the AFM [the regulator]. So, what you can see within our firm is a threshold emerging to participate in tenders run by municipalities who have been with a small audit firm, because supervision of those firms by the AFM is minimal or non-existent.

Although no specific registration requirements apply for Dutch auditors undertaking local public audit work, having an audit partner with experience in municipal audit was perceived crucial by interviewees for a firm to succeed in what was generally considered a very challenging area of audit, according to some the most complex sector to conduct audits. Several interviewed auditors explained the complexity of municipal audits by referring to the high regulatory intensity in which Dutch municipalities operate, and the political dimensions involved. The complexity of municipal audit is exemplified by the unsuccessful and short-lived track record of small audit firms attempting to enter the Dutch local audit market without staff sufficiently experienced in municipal audit (e.g., Vallei Accountants, see also Table 4). For newly entering firms, however, acquiring auditors experienced in local audit was generally not considered a major challenge by interviewees given the market retreat by Big-4 firms, which has caused a surplus of LG auditors in those firms, easing recruitment of experienced LG auditors by small and mid-tier firms. Given that this is a temporary effect linked to the recent market withdrawal by Big-4 firms, some interviewees questioned the future ability of the market to continue to deliver high-quality LG audit staff, as the infrastructure to do so is often more restricted outside the Big-4. However, there are signs of increased collaboration amongst non Big-4 firms active in Dutch municipal audit, which, in addition to being aimed at increasing geographical coverage, is focused on developing a LG audit expertise infrastructure which goes beyond what could feasibly be provided by smaller firms individually.

The statutory requirement in England for audit firms seeking to undertake LG audits to register with the ICAEW, and the limited pool of KAPs available to lead LG audits, has considerable influence on the English local public audit market, and poses a challenge particularly for small firms. In the Netherlands, in contrast, supplier power is comparatively

weak as no formal requirements are in place of having to possess specially licensed senior staff. This reduces costs for Dutch audit firms active in local public audit, and particularly eases market access by new entrant firms.

6.2 Threat of entry

Several barriers to market entry by new firms can be identified in the English and Dutch LG audit markets. These include barriers related to the requirements on minimum audit firm size and the procurement process, and technical and regulatory barriers. Despite the existence of these barriers in both countries, their impact differs significantly, with the barriers being more substantial in England compared to the Netherlands.

6.2.1 Requirements regarding minimum audit firm size

In England, a key entry barrier for small firms wishing to take part in PSAA's tender process is the audit firm size requirement used by PSAA in its audit procurement. In line with the principles set out in the FRC's Ethical Standard (4.24), PSAA does not award contracts to firms if their annual income from the contract would exceed 15% of the total annual fee income of the firm (PSAA, 2017a). Firms wishing to tender for PSAA's smallest substantive lot – sized £2.2m – would need to have an annual turnover of greater than £14.7m.

The use by PSAA of relatively large minimum lot sizes, which followed market engagement work by PSAA with the approved suppliers, automatically excludes small firms from tendering for PSAA contracts and reduces the pool of 'eligible' firms for these contracts to the around 40 UK firms with a turnover of £15m or more (Accountancy Age, undated). Small firms specifically identified the size of the lots as a barrier to entry and that they would only be interested in smaller lots (Touchstone Renard, 2020). One firm that was interested in tendering for LG audits noted that as their turnover was only £3m, they could only tender for a contract worth up to £0.45m.

The FRC's Ethical Standard (4.24) has been similarly incorporated by the Dutch accounting profession, however as an individual municipal audit contract rarely makes up more

than 15% of a firm's total annual fee income, the regulation constitutes only a minor barrier in practice.⁴⁵

6.2.2 *Impact of procurement framework*

A further difference in entry barriers related to the audit procurement is that in England, PSAA did not allocate firms to individual audits until the tender process was complete. While the PSAA Invitation to Tender requested that tenderers identify the location of their centres of excellence in local auditing (PSAA, 2017b), there was uncertainty about the location of any audits won until the results of the allocation process were announced. Several successful tenderers expressed a preference for more regionalised lots, which would better enable them to develop (or maintain) public audit expertise centres or prevent having to implement significant rotation of staff across the country. In a subsequent review, six out of the nine firms approved by PSAA said that they would like to see a larger number of smaller lots and that the 40% and 30% lots had proved excessively challenging for firms in terms of size and demand and that no lot should be greater than 20% of the total (Touchstone Renard, 2020, p. 13). Similarly, non-registered firms indicated they would be more interested in local lots with some stating they would only consider participating in future tenders if smaller lots were available. An interviewed auditor at a small firm commented:

It was very difficult to do. Unless, again, you had a lot of offices that already did this type of work across England, then you were having to make, as I say, a lot of assumptions about where the work may be based. So again, it very much favours the incumbent.

Several existing suppliers identified a further difficulty arising from PSAA's practice of not allocating firms to individual audits until the tender process was complete, namely the lack of advance information on the composition of the lots. As a result, they could not base their tender prices and resources planning on the characteristics and risks of each individual audit for which they were bidding, and this gave rise to increased commercial risk. As a result, firms said that

⁵ Section 5.2, Verordening inzake de onafhankelijkheid van accountants bij assurance-opdrachten (ViO) (2014), NBA.

if they have to bid ‘blind’ again in the next procurement round, they would increase their prices to cover unforeseen risks (Touchstone Renard, 2020). This approach taken by PSAA to the procurement using large national lots was key to the results and the different evolution of the English and Dutch markets. The approach reflected a long-standing professional logic in audit firm appointments which had remained dominant despite blending with the newly imposed market logic. An interviewed PSAA official commented:

The starting point is the most important thing in everything here, is we must be able to appoint an independent auditor. We knew, from my own experience and Audit Commission experience, that at some councils, there were four or even five firms that were conflicted and couldn't be the independent auditor [-]. The whole of the officer team advocated quite firmly about going on a national basis.

With most audit contracts procured by individual municipalities, auditors in the Dutch system face minimal uncertainty as to the location of their future audit work. This lesser uncertainty significantly reduces firm entry barriers in the Dutch system. It also contributes however to smaller municipalities, or those based in more peripheral regions, struggling to attract market interest as firms' profit margins on these audit contracts tend to be smaller. This is shown by the four municipalities that did not receive a single submission to their audit tender in 2016 all being small authorities with less than 20,000 inhabitants and based in the sparsely populated north-eastern part of the Netherlands (BZK, 2017).

Although uncertainty regarding the audit location is minimal, several interviewed Dutch auditors referred to uncertainty arising from the way in which many Dutch municipal audit contracts are procured. Many municipalities, particularly those tendering contracts subjected to EU procurement rules, do not facilitate potentially tendering firms to approach municipal officials prior to submitting their bid. Auditors indicated this made it difficult to ‘get a feel’ as to whether the municipality would fit with the audit firm's profile and to gain sufficient insight into the quality of the municipality's internal administrative organisation. As the latter significantly affects the workload required for the eventual audit, several auditors felt an EU compliant procurement is often inadequate to gather information they perceived essential in order to determine whether to submit a bid. This view was articulated particularly by firms with less experience in the local audit market which had limited knowledge of the various reputations held by municipalities. Smaller municipalities in contrast generally facilitate information exchange between (potentially) tendering firms and municipal officials,

and small firm interviewees indicated their firm generally only participates in tenders if the ability exists to gather information on the municipal administrative organisation in addition to what is included in what auditors generally regarded as rather uninformative municipal procurement documents.

6.2.3 *Technical barriers*

In both England and the Netherlands technical barriers exist and mainly relate to special reporting requirements applying to LGs.

In England, LG financial reports are compiled in accordance with the CIPFA LG code, a heavily modified version of IFRS. The complexity of the code is not specifically seen as an issue by non-registered firms, but they recognised that adapting to its requirements would result in additional costs, which would be required to meet the work involved in understanding the sector and the risks, preparing audit programmes and investing in technology (Touchstone Renard, 2020). One small firm, whilst recognising the unique technical aspects of LG audit, considered that their audit approach is designed to suit any client in any sector, hence considering the technical barriers of LG auditing to be low. One interviewed auditor, whose firm decided not to take part in PSAA's tender in 2018, commented:

We clearly were not experienced enough to know how to make a decent turn on a public sector contract.... So part of our challenge, I think, for those of us that are coming in new is to understand how the system works and how to make it pay, while maintaining the quality requirements.

Dutch municipalities use a special accountancy code called the BBV. The BBV was introduced in 2004 and renewed the previous regulatory framework which explicitly used Dutch GAAP as a reference point (Bac, 2002; Budding & Van Schaik, 2015). The current standard setting role of the BBV is provided by a special interpretations committee – *the Commissie BBV* –, which includes representatives of central and subnational government, and audit firms. Although the BBV itself was perceived by most interviewed auditors as ‘not particularly complicated’, the special accounting features of municipalities resulting from their many revenue and expenditure streams were seen as adding significantly to the technical complexity of municipal audit work. Audit complexity has increased following major decentralisations of social welfare tasks to the Dutch municipal level in 2015 (De Widt & Laffin, 2018). The

increased audit complexity has increased cost pressures for auditors and has contributed to a growing number of conflicts between auditors and municipalities about extra charges.

A recent survey also shows that Dutch auditors perceive audits at LGs as more complex compared to audits of small and medium-sized enterprises (SEO Amsterdam Economics, 2019). Further, the application of the BBV as a special audit code applying to Dutch subnational authorities not only complicates movement of auditors from private sector audit into municipal audit, but also from auditors active in other parts of the Dutch public sector, which do not report according to the BBV. However, the BBV constitutes a smaller entry barrier compared to the IFRS based reporting rules applying to English LGs' given the BBV's relatively small size.⁶

6.2.4 Impact of increased regulatory scrutiny

In England, under the transitional arrangements established by the 2014 Act, PSAA was responsible for monitoring the quality of local audits undertaken by the audit firms. PSAA's work included commissioning the FRC's Audit Quality Review Team (AQRT) to inspect financial statements opinion files and VFM arrangements conclusion files across each firm's work. The AQRT also provided a commentary on the applicability of firm-wide procedures to the PSAA audits (PSAA, 2019). From 2018/19 the transitional arrangements came to an end and the definitive arrangements required by the 2014 Act came into force. The FRC is responsible for the overall inspection regime and undertaking inspections of major local audits, which includes both LG and health bodies (excluding NHS Foundation Trusts) with either revenue or expenditure in excess of £500m, whilst the ICAEW is responsible for monitoring other audits. For the audits of the 2018/19 accounts, the FRC reviewed the audits of 15 of the 271 bodies that meet the definition of major local audits. Twelve of the audits were of LG bodies, where the auditors were appointed by PSAA, while three audits were outside the PSAA regime. The FRC's reported results of the quality of audit reviews, which do not differentiate between PSAA appointed auditors and audits of health bodies, show that the FRC labelled 40% of the reviewed audits 'good', or requiring 'limited improvements', whilst the other audits were identified as 'requiring improvement' (47%), or 'significant improvement' (13%). The FRC concluded that:

⁶ The 2007 IPSAS manual has 1,071 pages, whilst the BBV contains including additional notes, Information for third parties (Iv3) and Q&A's at most from half that number of pages (Committee BBV, 2008).

Urgent action is required from some of the firms to take appropriate action to respond to our findings to ensure improvements are made in audit quality, given the deterioration in quality in the year.’ (FRC, 2020, p. 4)

As a result of the system used by PSAA to allocate audits to firms, it is likely that each of the firms has a number of major audits, and each is therefore likely to be subject to regular review by the FRC. The FRC regime is regarded by current suppliers to PSAA as being more onerous than the previous arrangements (Touchstone Renard, 2020). Several interviewed auditors expressed concern that as the quality standards increase, and the regulatory environment is ‘getting much more pointed’, this gives rise to significant reputational risks while simultaneously fee rates have reduced. As the regime has become tougher, the balance of risk and reward has changed since firms bid for PSAA contracts in 2017. As a result, firms’ commitment to remaining in the LG audit market is uncertain and dependent on developments ahead of the next procurement round.

Non-registered firms also stated that ‘the FRC is a tough regulator. If your file gets picked, it can add 20-25% to time and costs (for that audit)’. External reviews increase time and costs, and auditors state they would look for higher fees to compensate for these risks (Touchstone Renard, 2020). One interviewed unregistered auditor noted that while the new regulatory regime reflects the regime already in place for the private sector, the challenge of the FRC regime, which involves public reporting, means that ‘this is not an area you’re going to go into to only have one or two clients’. In addition, central government enforced austerity cuts have similarly put pressure on auditors’ work, making audits more demanding as English LG financial risks have increased, causing ongoing pressure on audit fees. This has made LG audit work less attractive, especially for firms with a higher cost level such as the Big-4.

In the Netherlands, the Minister of Finance has delegated quality supervision of all registered accounting firms to the Netherlands Authority for the Financial Markets (AFM). In practice, the AFM concentrates its supervision on accounting firms with a public interest licence, which besides the Big-4 includes BDO and Mazars. Supervision of all remaining accounting firms is primarily conducted by the Royal Netherlands Institute of Chartered Accountants (NBA), and the Association of Chartered Accountants (SRA). Although interviewees demonstrate mixed views regarding the manner in which the AFM conducts its supervisory role, nearly all interviewees emphasise that the AFM’s role is critical to understand withdrawal by the large firms from the Dutch local audit market. Following its foundation in 2002, the AFM published its first extensive reviews into the audit quality delivered by Big-4

firms in 2010 (AFM, 2010), which covered the financial year 2009/10. This was followed by reviews of the audits over the years 2012/13, and 2014/15, with each review encompassing municipal audits (e.g., AFM, 2014). With KPMG already having left the market, the AFM reviewed three municipal audit cases from each of the remaining Big-4 firms active in municipal audit. Out of the nine cases reviewed over the entire period, the AFM rated the audit quality compliant for only one dossier (held by PwC). Interviewees indicate that the AFM quality reviews and the subsequent significant negative publicity they caused, triggered a strategic reorientation amongst the large firms regarding their role in municipal audit. A senior Deloitte auditor comments:

2014/15 was a striking moment – the AFM reviews [of the 2014/15 audits] arrived in Spring 2016, and PwC, Deloitte, and EY again did not pass. PwC then implemented major changes, EY said completely farewell to the market at that time, and we also drastically changed course. The biggest issue we identified for the non-compliance of our cases is that we had a capacity problem – we then said ‘from now onwards we are only going to submit a bid if we have capacity and if we can guarantee the quality of the work by getting an adequate audit fee’.

The AFM reviews not only triggered major shifts on the Dutch municipal audit market but also led to a reinvigoration of firms’ LG audit practices. Most interviewees indicate that the AFM’s scrutiny has had a positive impact on the quality of Big-4 municipal audits, as it forced firms to address what most interviewees, including those based at large firms, perceived to be genuine shortcomings in the then quality of municipal audit. Some interviewees however criticised what they perceived to be an overly formalistic supervision approach by the AFM which pushed auditors’ work into a ‘box-ticking exercise’ (interview municipal finance official, previously Big-4). In many cases, interviewees positively contrasted the audit quality reviews by the professional bodies – NBA and SRA – with those of the AFM, with the former ostensibly applying a more pragmatic and less formalistic approach to audit quality reviews.

Another point of criticism concentrated on the AFM’s initial regulatory focus on the audit quality provided by Big-4 firms, who subsequently felt being ‘picked out’, as put by one Big-4 auditor. More in-depth reviews of mid-tier firms followed a couple of years later, and as some of their results were equally critical for some mid-tier firms, multiple interviewees

pointed at the AFM's regulatory scrutiny to explain the decreasing market share of some mid-tier firms post-2016 (e.g., Baker Tilly Berk).⁷

Enhanced regulatory scrutiny of the quality of municipal audits similarly put pressure on firms' internal discussions. Multiple interviewed audit partners, from Big-4 but also mid-tier firms, stated that the enhanced regulatory scrutiny incentivised a strategic reorientation by their firm in relation to municipal audit. In some firms, this subsequently resulted in a deliberate decision to abandon the local public audit market, whilst others made a strategic commitment to the sector, even with the knowledge this would require additional investments and consume staff resources which their firm could allocate to more lucrative private sector audits. In order to explain firms' strategic commitment to local audit, interviewees referred to professional rather than commercial logics as guiding their firms' decision-making. One Big-4 partner noted:

We have traditionally played an important role in the public sector, in all segments [-]. So, our board of directors said very explicitly 'we must take our social responsibility by continuing to play a role in the [municipal] sector' and, secondly, we strongly believe in a full-service concept and then you cannot exclude one market segment [-] because you believe it is less profitable.

However, despite the strategic commitment made to local audit by some Big-4 firms, these firms have become increasingly focused on serving larger municipalities, which tend to allocate a higher weight to quality in their audit procurement and are willing to pay a higher audit fee. Hence although the involvement of some of the large firms with municipal audit reflects a professional logic, these logics have become blended more strongly than previously with a commercial logic.

The impact of the different approaches by Dutch regulators to reviewing audit quality appears substantial on the Dutch municipal audit market. Several interviewees indicate auditors at small firms are able to operate in a less formalistic way partly because they are not being subjected to AFM supervision, which enables them to apply an audit approach which better matches the auditor profile often sought after by especially smaller municipalities who value a certain flexibility when interacting with their auditor. An example of such flexibility provided

⁷ A quality review published by the AFM in 2017 strongly criticised audit work delivered by Baker Tilly Berk – out of ten review areas, seven areas were evaluated as 'lagging far behind expectations', one as 'lagging behind expectations', and two as 'almost conform to expectations' (AFM, 2017, p.40).

by an auditor is that their small firm, unlike Big-4 auditors, is able to provide a degree of timetable flexibility in the scheduling of their audit activities, as is sometimes requested by the audited municipality. The interviewee explained their firm's flexibility by referring to small businesses constituting their firm's other major client base, and if needs come to, these businesses would often be willing for their audit to be rescheduled if this would enable the audit firm to accommodate timetable changes requested by one of its municipal clients. As auditees of the Big-4 are often major, stock listed enterprises subjected to a strict audit schedule, auditors at large firms are generally far less able, through internal redeployment of audit staff, to accommodate municipal requests for changes to their scheduled audit. We also found hints that some municipalities may prefer a small auditor, as this would result in a 'less rigid' audit. However other interviewees, including those based at small firms, disagreed and stated their audit was not of lesser quality than those provided by large firms. Nonetheless, it was felt by most interviewees, including auditors at small firms, that LG audit expertise is potentially more vulnerable at small firms since it is often held by a single or small number of people.

6.3 The power of buyers

In England, although presently there are 494 potential buyers for LG audit, in practice there are only 11 buyers: ten individual local authorities and PSAA who is the predominant buyer with 98% of the market. Concentration of buyers is reinforced by the requirements of LG audit, which as a consequence of being highly prescribed by legislation and professional requirements, is a standardised product, and buyers incur low costs in changing suppliers. The effect of buyer concentration is further reinforced by the financial situation of English LGs which have experienced considerable financial pressure since the global financial crisis ((accumulating to a 49.1% real-terms reduction in central government funding between 2010/11 and 2017/18 (NAO, 2018)). Following Porter (2008), and also taking into account the peripheral nature of audit to English LGs (De Widt et al., 2020), and perceived low switching costs, this could be expected to result in a focus on price rather than quality. In its 2018 procurement of audit contracts, PSAA weighted price equally with quality and the procurement saw prices reduce by a further 23% following previous cumulative reductions of 65% since 2010 (albeit these also reflected reductions in audit scope and the costs of running the Audit Commission) (see section 4.1). However, interviewed auditors from the firms participating in the procurement observed that in practice the method of quality evaluation lacked depth as it relied on simply a review of the quality documents submitted by tenderers. One firm said that

‘we don’t believe you can differentiate on a questionnaire basis (the) true quality of the teams’. This meant all firms could meet the quality requirements, effectively meaning supplier selection tended to depend more on price.

The importance attached to price during the procurement of local public audit contracts is also visible in the period before PSAA – e.g., the quality:price ratio used by the Audit Commission was 40:60 – which might reflect what has historically been a strong emphasis in English LG on efficiency considerations. The central role of an efficiency imperative (Martinez & Dacin, 1999) is also visible in the lobbying by the LGA with central government to enable the English local sector to develop a collective scheme for the appointment of local auditors. Whilst reflecting upon the originally intended regime, as set out in the draft of the 2014 Act, which assumed each LG would individually procure their audit contract, an interviewed LGA official noted:

From day one, I and others here felt that this wouldn’t necessarily be the most efficient. This is one area where we were probably, as an organisation, argue much more about a national offer, whereas for most other parts of the delivery of local government we make the case for localism. That each council is different, the localities are different, they should be allowed to look at things from a local perspective and, if necessary, procure things locally. In this area [local audit] because it’s so nationally prescribed [-], we always felt an offer around national procurement made sense.

Some stakeholders however (e.g., CIPFA and the FRC) were more critical of the efficiency imperative and saw the setup of a national procurement scheme, combined with the continuation of the central level appointment of local auditors, as inhibiting local level engagement with the external audit function, and contributing to what they perceived as a narrow focus by local actors on audit costs.

The concentration of buyer power via PSAA also had a further effect, in that the size and composition of lots made it harder for some smaller firms to compete effectively. Buyer power in England is therefore very high and the procurement approach taken by the predominant buyer may have stimulated further concentration in the market, reducing the potential further for new entrant, small firms. In the Netherlands, buyer power is relatively weak as most LGs appoint their own auditor, resulting in relatively small purchasing volume of individual buyers. There are also perceptual differences in quality of audit provided by auditors. Audited bodies in England, while recognising the possible need to attract smaller

firms into the market in order to maintain competition, expressed the view that smaller firms would not have the technical skills, training or capacity to deliver LG audits (PSAA, 2018).

Perceptual differences are relevant in the Netherlands too, however not only to the benefit of large firms, as some small firms have built a strong reputation for their perceived expertise and quality of conducted local public audits. These differences reduce LGs' negotiating power, as there will be less opportunity to play one firm against another. To enhance buyer power, the suggestion has been put forward municipalities procure their audit contracts collectively, something currently practiced by a minority of Dutch LGs. An obstacle raised in this regard was what several interviewees referred to as the 'rather autonomous attitude' amongst many Dutch municipalities. This bureaucratic logic of municipalities, which reflects the Dutch system's decentralised-unitary nature, complicates developing a collective procurement exercise, especially at a larger, potentially national scale. To enhance buyer power, the Dutch Association of Municipalities developed a guidance in 2017 to help municipalities in procuring their audit contracts, and ensure municipalities receive sufficient bids. The guidance incentivises municipalities to reconsider inclusion of the selection criterion 'experience'; to procure audit contracts of a sufficient length (at least three years); and to avoid a procurement design where the lowest bidder automatically wins the contract (VNG, 2017).

A key feature that has increased bargaining power of Dutch LGs over the past two decades is the introduction of compulsory procurement rules, which increased the power position of municipal purchase departments, and, as a result, made Dutch LGs more price sensitive in the selection process of auditors. Due to this, audit work has increasingly been perceived by LGs as standardised or undifferentiated, reducing the perceived switching costs for LGs and making it more difficult for auditors to compete, e.g., based on the claimed quality of their audit, subsequently reducing auditors' negotiating leverage. Further, many Dutch audit firms also provided non-audit services to the same municipality they were auditing, and multiple interviewees indicate that firms in their price war were willing to compromise significantly on their actual audit fee as they were able to generate substantial additional revenues 'once having a foot in the door of the municipality', as put by one interviewed auditor. This practice of 'one-stop shopping' included the provision of different types of services, such as HR services, with staff of the firms deployed at the municipality for longer periods of time. Even though unrelated to the actual audit, bonuses related to the provision of non-audit services were allocated to the partner responsible for the audit, under the title 'cross-selling'. Interviewees indicate that following internal and external pressures, 'one-stop shopping'

largely disappeared which has incentivised large firms to deprioritise municipal audit work and move towards more profitable private sector audits.

With municipalities experiencing rapidly declining interest by large audit firms, exemplified by some municipalities not receiving any submissions to their audit tenders (Knoop & Kakebeeke, 2017), many municipalities have seen it necessary to increase auditor's compensation. This is reflected in our review of municipal audit procurement documents (section 5.2), which shows an increasing weight allocated by municipalities to the quality ratio in their evaluation of tender bids, from an average of 58% in 2016 to 68% in 2019. Quality is measured by municipalities in different ways but commonly requires firms to submit both written tender submissions and participate in an interview or presentation at the municipal offices, with tendering firms generally ranked on the basis of their planned audit approach, their likely advisory potential, and the proposed composition of the audit team.

Interviewed auditors confirmed the greater importance Dutch municipalities now attach to quality, and how market pressure has increased municipal audit fees. Whilst audit fee figures are not publicly available as Dutch municipalities are not required to report them, all interviewees highlighted the substantial increase in audit fees in recent years, with auditors indicating there has been a doubling to tripling in average audit fees over the period 2017-20. Overall, and in comparison to England, buyer power in the Netherlands can be considered weak albeit this is starting to change following the recent increase in audit fees.

6.4 Threat of substitutes

Porter claims that a substitute 'performs the same or a similar function as an industry's product by different means' (Porter, 2008, p 31). In both England and the Netherlands, professionally qualified auditors carry out local audits in accordance with legislation and professional standards. Various changes have been made in both countries to the requirements for LG audits in the recent past, such as the reduction in the level of performance auditing in England in the early 2000s and the removal of the requirement for Dutch auditors to assess the legality of municipal spending decisions (effective from 2021). Despite these changes, and intensifying discussions in both countries as to the adequateness and effectiveness of local public audit, it appears unlikely that the current audit requirement will be substituted by another type of service in the medium term.

Whilst the audit requirement is unlikely to change, limited supply on the Dutch local public audit market has resulted in Dutch LGs and policymakers actively looking for the municipal audit to be conducted by other organisations than the current private sector audit

firms. The Dutch Interior Ministry and Association of Dutch Municipalities have suggested municipalities could follow the example of Amsterdam and The Hague and establish their own audit service, possibly in collaboration with neighbouring municipalities (BZK, 2017; VNG, 2020). However, most interviewees considered this unrealistic given the continuous scarcity of accountants, which would impede recruitment, whilst others thought it was undesirable too given the lower independence of auditors if based within the municipal organisation. Although the audit service itself will not be substituted if a growing number of Dutch municipalities do indeed decide to set up a municipal audit service, such a shift will evidently reduce demand for audit services currently provided by private sector firms.

Overall, the direct threat of substitution of the audit service is low in both England and the Netherlands, although in the Dutch case alternatives to private sector audit provision are being considered by a growing number of municipalities.

6.5 Rivalry among existing competitors

Differences in procurement appear to be at the root of the significantly different competitive dynamics observable when comparing the Dutch and English local audit markets. In England, the tender evaluation process used by PSAA as part of its 2017 procurement exercise gave equal weighting to price and quality. However, as all the firms, with one exception, who submitted tenders were able to meet the quality criteria, audit firms considered that success in the procurement was largely dependent on price. Whilst some large firms were willing to compete vigorously and reduced audit fees in order to win a share of the LG market, others, who had been involved in LG audit in the past, failed to receive a contract from PSAA (KPMG) or did not even bid (PwC) (Calkin, 2019). In addition, all registered firms stated that due to changes in the audit environment since the date of PSAA's tender, fees are now too low and LG audits are far less profitable than other types of external audit. As a result, fee rates in England are perceived by audit firms as not offering adequate rewards to compensate for the risks firms perceive they are taking and that their continuing involvement in the market is conditional. Partners in other parts of the firms are questioning whether LG auditing is worthwhile, in terms of risks and rewards, for the firm as a whole. A public sector audit partner in one registered audit firm commented:

the real risk is potentially... of [the firm's leadership] just saying, "commercial return here is so poor, and the regulator is being so difficult, and we've got so little flexibility because the price is in essence fixed for five or seven years." That is a big question

because there are big reputational issues here. It's very easy for [the firm's leadership] just to say, high level of percentage on price, risk reward is just wrong, don't bid it.

Similarly, amongst interviewed non-registered firms we found limited enthusiasm about bidding for work in the next round of procurement, findings that have similarly been identified in a PSAA assigned review of future audit supply options (Touchstone Renard, 2020). The downward pressure on English LG audit fees has been such that the Redmond Report (2020, p. 72) concluded 'that audit fees are at least 25% lower than is required to fulfil current local audit requirements effectively'.⁸

In the Netherlands, instead, recent increases in audit fees are enhancing the commercial attractiveness of the market. Most interviewed Dutch auditors indicate that, on average, the current fee levels in place are making the market commercially sufficiently rewarding. This is also illustrated, for example, by EY currently seeking to re-enter the municipal audit market. Nonetheless, Dutch municipalities on average have continue to experience less choice when appointing their auditor compared to other industries. A survey by SEO Amsterdam Economics (2019) shows that 52% of the surveyed municipalities (and provinces) indicate having little or no choice when selecting a new audit firm, compared to 32% in other sectors. However, several interviewees expected that following the economic impact of the COVID-19 pandemic, audit firms may increase their efforts to acquire municipal clients given their more stable and solvent outlook compared to many private sector clients.

Overall, competitive rivalry in the Netherlands is moderate due to large firms being focused on the limited number of large Dutch LGs; but it may be increasing as new entrants arrive who may have a lower cost base and look for additional contracts. The large contracts available in England have kept the local public audit market relatively attractive for most big players and has resulted in a highly competitive market. When confronted during the interviews with the English model, responses amongst interviewed Dutch auditors where highly mixed, including amongst Big-4 firms, with some attracted to PSAA's national level procurement approach as a way to reduce transaction costs of what are perceived as time consuming municipal audit procurement processes, whilst others feared it would lead to an overconcentration on price. However, the continuing reduction of audit fees has significantly

⁸ Four of the firms suggested that an increase of between 15% to 25% on the scale fee is required with the fifth firm requesting an increase of 100% on the scale fee (Redmond, 2020, p. 24).

reduced the profitability for firms active in English local audit and there are indications that competitive rivalry will be reduced in future.

Table 9 summarises our main findings for the five forces, and illustrates important differences depending on whether one applies a short term versus medium to long term analysis when identifying market differences. For example, whilst power of buyers is currently strong in England and weak in the Netherlands, differences are likely to become smaller when applying a longer-term perspective, as buyer power is likely to weaken in England, whilst it is likely to increase in the Netherlands.

- *Insert Table 9* -

7. SUMMARY AND CONCLUSIONS

In this paper, we apply Porter's five forces framework and institutional logics to analyse market trends in LG audit in England and the Netherlands. Despite moves towards market liberalisation in both countries, they have taken different paths with different effects in terms of market competition, concentration and the presence of small firms.

To summarise, the threat of entry by new firms is low in England due to requirements regarding minimum firm size, uncertainty regarding the location of audits and LG specific technical requirements for LG audit firms. The Netherlands has much lower entry barriers, and so higher threat of entry by new firms, as contracting is done individually for a known LG client and the LG specific technical requirements are less demanding. Whilst LG audit expertise is considered essential for entering firms in England and the Netherlands, acquiring auditors with LG audit expertise is not an unsurmountable challenge in either country following the abolition of the Audit Commission in England and withdrawal from the market by Big-4 firms in the Netherlands.

The power of suppliers is expressed in England via stringent registration requirements for LG audit required by legislation and the FRC which effectively means that audit firms have to draw key audit partners undertaking LG audits from a small pool of suitably qualified and experienced staff, and so increases the barriers to entry for small firms. There is no similar requirement in the Netherlands.

The power of buyers emerges as the most salient force. In England this is due to the existence of the collaborative purchasing scheme PSAA, further emphasised by the use of large sized lots and strong continuing pressures on prices, which have discouraged small firms.

However, in the longer term reducing firm interest in LG audit might pose a significant challenge to buyer power in England. In the Netherlands, buyer power is considerably weaker as most LGs continue to procure individually. The threat of substitution however appears stronger in the Netherlands due to current discussions about forming a municipal audit service, which would effectively substitute for private sector firms. This appears for now much less likely in England since such a public sector run service was recently ended as part of the market liberalisation process.

Competitive rivalry in England has remained strong due to the approach taken to procurement. However, this is now threatened due to on-going fee reductions leading to loss of interest by at least some incumbents and which has led PSAA to undertake a review of future supply options (Touchstone Renard, 2020). The Netherlands has experienced more moderate rivalry as larger firms have shown declining interest in the market, but this does appear to be increasing as new, smaller, firms continue to enter the market, and fee increases have renewed interest by some larger firms.

In conclusion, we find that the structure of the market in England, particularly buyer power, has served to encourage large firm concentration and discouraged new entrants especially smaller firms whereas in the Netherlands the disaggregated market together with lower barriers to entry has had the opposite effect of discouraging larger firms and encouraging new entrants and smaller firms. However, the approach in England has maintained large firm interest across the LG market compared to the Netherlands (8 tenders were received by PSAA in 2017; the average number of tenders to Dutch LGs in this study was 2.3) and supports the contention that concentration does not necessarily mean lack of competition and may even strengthen it. There is evidence that the English approach has constrained fee levels compared to the Netherlands, although insufficient evidence is currently available as to its impact on audit quality – providing an important area for further research.

Significantly though it is not solely the market structure but also the regulatory framework in place which explains recent market trends. For the Dutch case, enhanced regulatory scrutiny of municipal audits provides the main explanation for the market withdrawal by Big-4 firms in recent years. This supports previous suggestions (McGinn, 2010; Mahat, 2018) that the five forces may not in all industries give sufficient weight to the role of government, specifically its regulatory impact. Consequently, whilst the application of the five forces framework in this paper enables the identification of major market determinants, our country comparison demonstrates that for the analysis of LG audit markets there is a need to account more strongly for institutional and regulatory dimensions. These dimensions are both

internal and external to the local public audit field, and different institutional logics are observable amongst the investigated country cases.

England's approach suggests an example where different institutional logics of market, bureaucracy and professions have been blended at field level through PSAA as the pressure from government legislative reforms (the 2014 Act) - predominantly guided by a market logic - were accommodated with the predominant bureaucratic and professional logics in the LG community of external centralised audit appointments by the Audit Commission. This blending developed firstly in the successful lobbying of the LGA for the appointing person role followed by the approval of a LGA owned company (PSAA Limited) as an appointing person, and then in the internal dynamics of PSAA as staff recruited from the Audit Commission applied a procurement approach drawing on their Audit Commission experience, illuminating the primacy of independence in audit appointments and the use of large, national lots.

Whereas PSAA provides an example of blended hybridisation (Skelcher & Smith, 2015, p.442), in the Dutch case, individual municipal audit appointments continued following the liberalisation of VB Accountants, highlighting a higher level of continuity in the Dutch system's underlying logic. The fact that prior to liberalisation most Dutch municipalities were (voluntarily) audited by VB Accountants, being a relatively small firm focused on public sector audit, contributed to a culture in which Dutch municipalities developed an appreciation for specialised public sector auditors. This gave rise to a professional logic which emphasised the relevance of auditors holding local public sector expertise, irrespective of the firm size in which they are based. The persistence of this logic helps to explain why notwithstanding the market withdrawal by Big-4 firms in recent years, the focus of actors in the Dutch system has been on resolving capacity issues whilst shifts in the size of firms involved in municipal audit received far less attention. This contrasts with England, where LGs have always had their auditor appointed by an external body, in most cases resulting in the audit being conducted by a large organisation, either the Audit Commission or a large accountancy firm, inducing a preference amongst English auditees for large firms.

Our findings highlight the historically contingent nature of decision-making by individuals and organisations operating within the Dutch and English markets, which appears critically affected by the period prior to the liberalisation of their local public audit markets. Although historical legacies do not predetermine actors' agency, they substantially influence actors' assumptions and values in relation to local public audit, and appear critical to illuminate the diverging trajectories of the two countries analysed. In England, the historical contingency of the professional logic is visible in the appointment of an auditor by a body external to the

LG – PSAA in the current setup – being perceived as legitimate and the appointment of a large firm as most appropriate. In contrast, as a ‘match’ between a municipality’s profile and that of its audit firm has historically been valued, Dutch municipalities have continued to make their own auditor appointment, even with the knowledge that a collaborative procurement approach would likely generate efficiency and cost benefits.

The findings of this study demonstrate the value of investigating shifts in local public audit markets as a way of understanding the broader institutional logics underlying systems of local public audit. Whilst our study traces different logics across the country cases and time periods investigated, further research amongst a larger number of country settings but also different segments of the public sector promises to provide further vital insights into the origins and evolution of auditors’ and auditees’ logics in relation to local public audit, and the extent to which these relate to different institutional environments. For example, different levels of decentralisation may influence local views and practices in use for the appointment of local auditors, and whether auditors are mostly private or public sector based. Of particular interest here is developing the concept of hybrid organisational forms as competing institutional logics arise, so far predominantly applied to the third sector (Skelcher, C., & Smith, 2015). Micro level empirical study of public sector organisations in contexts where market, bureaucratic, professional or other logics have collided as result of external changes – typically government policy – would strengthen understanding of how logics evolve whether via blending or other accommodations.

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Data Sharing

The data that support the findings of this study are available from the corresponding author upon reasonable request. The data are not publicly available due to privacy or ethical restrictions.

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Table 1: Allocation of English local public audit contracts by value

	AUDIT COMMISSION (AC) LET CONTRACTS ¹				CONTRACTS POST 2014 ACT ²	
	2010/11		2012/13		2018/19	
	£m	%	£m	%	£m	%
AC IN-HOUSE	124.8	72.3	0.0	0.0	0.0	0.0
BIG-4	31.0	18.0	74.1	52.8	13.5	36.2
Deloitte	7.0	4.1	30.1	22.7	2.2	5.9
KPMG	12.2	7.1	12.2	7.1	0.1	0.3
PwC	11.8	6.8	11.8	6.8	0.0	0.0
EY	0.0	0.0	20.0	16.2	11.2	30.0
MID-TIER	16.9	9.8	63.2	47.2	23.8	63.8
Grant Thornton	12.2	7.1	53.5	40.5	14.9	39.9
PKF	4.7	2.7	4.7	2.7	0.0	0.0
BDO	0.0	0.0	0.0	0.0	2.3	6.2
Mazars	0.0	0.0	5.0	4.0	6.6	17.7
TOTAL	172.7	100.0	137.3	100.0	37.3	100.0

Notes:

¹ Audit Commission let contracts:

- 2010/11 audit regime was far wider and included extensive VFM audit;
- 2010/11 and 2012/13 tenders include NHS bodies (excluding Foundation Trusts).

² These comprise contracts for the audit of 484 authorities let by PSAA and 10 by individual authorities.

Table 2: Details on stages of PSAA's procurement process

Number of firms/consortia submitting a selection questionnaire	10
Number of firms/consortia invited to tender	9
Number of firms/consortia submitting a tender	8
Number of firms/consortia awarded a contract	6

Source: PSAA 2018

Table 3: Firms active on the Dutch municipal audit market, 2013, 2016, and 2019

	2013		2016		2019	
	N	%	N	%	N	%
	LGs	LGs	LGs	LGs	LGs	LGs
TOTAL DUTCH LGS	407	100	390	100	355	100
Auditor (firm's total turnover in the Netherlands in 2019, in million euros)						
BIG-4	363	89.2	184	47.2	84	23.7
Deloitte (1,015.5)	175	43.0	87	22.3	57	16.0
EY (905.0)	132	32.4	67	17.2	1	0.3
PwC (949.8)	56	13.7	30	7.7	26	7.3
MID-TIER	31	7.6	152	39.0	152	42.8
Baker Tilly Berk (96.1)	28	6.9	80	20.5	67	18.9
BDO (293.8)	1	0.2	60	15.4	62	17.5
Crowe Foederer (51.4)	0	0.0	0	0.0	14	3.9
RSM (60.0)	2	0.5	4	1.0	8	2.2
Mazars (111.8)	0	0.0	8	2.0	1	0.3
SMALLER FIRMS	9	2.2	52	13.3	117	33.0
(see Table 4 for details)						
MUNICIPAL	2	0.5	2	0.5	2	0.6
AUDIT SERVICE						
Amsterdam,						
The Hague						
Unknown	2	0.5	-	-	-	-

Source: own composition, multiple sources including www.accountant.nl, BMC (2016) and BZK.

Table 4: *Number of Dutch LGs audited by smaller firms – number of municipal audit contracts by firm*

	2013	2015	2016	2017	2018	2019
A12	0	0	0	0	0	1
Astrium	0	0	0	13	21	26
Blue Line	1	1	0	0	0	0
Eshuis	0	0	0	3	3	4
Hofsteenge Zeeman	0	9	22	28	23	21
IPA-Acon	7	11	15	17	18	18
Konings & Meeuwissen	0	0	0	0	0	1
KSG	0	1	1	2	5	6
Q-Concepts	0	0	1	1	1	5
PSA	0	0	0	5	9	16
Stolwijk Kelderman	0	0	3	4	9	9
Vallei	0	0	5	0	0	0
Verstegen	1	3	5	7	7	10
<i>TOTAL N LGs</i>	9	25	52	85	102	117
<i>% OF TOTAL DUTCH LGS</i>	2.2	6.4	13.3	21.9	26.8	33.0

Source: own composition, multiple sources including www.accountant.nl, BMC (2016) and BZK.

Table 5: Allocation of English local public audits by category of audited body

Audit firm	Allocated audits by category of audited body 2018/19												Total number audits*	£ Average fee per audit	Total annual fee	
	Unitary authority	London Borough Council	Metropolitan district	County council	GLA	Combined authority	District Council	Chief Constable	Fire and Rescue Authority	Police and Crime/Fire Commissioner	Pension Fund	Other			£ million	% of total
<i>BDO</i>	1	4		1			12	3	1	3	5		30	51,069	1.53	5.4
<i>Deloitte</i>	4	2	1	2			16		4		7	1	37	48,715	1.80	6.4
<i>EY</i>	15	10	4	9	4	2	76	13	8	15	22	8	186	45,601	8.48	30.0
<i>Grant Thornton</i>	23	11	15	13		2	71	15	8	16	31	7	212	52,838	11.20	39.6
<i>Mazars</i>	10	5	14	2		5	25	6	5	6	11	7	96	55,130	5.29	18.7
Total	53	32	34	27	4	9	200	37	26	40	76	23	561	50,464	28.31	100.0

* The total number of audits differs to the number of opted-in bodies (494) due to authorities' pension funds being treated here as separate audits and certain other changes in the composition of audits due to abolitions, amalgamations etc. that took place after the PSAA tender exercise.

Source: PSAA Directory of auditors and scale fees for opted-in authorities <https://www.psa.co.uk/appointing-auditors-and-fees/list-of-auditor-appointments-and-scale-fees/> (accessed May 2021).

Table 6: *Variable names panel dataset English LGs, 2005-2016*

Variable	Measurement	Source
nonbig4	Equal to 1 in case of a non Big-4 audit firm appointment, 0 otherwise.	TenderNed.nl (online tendering platform)
tenders	Number of tender submissions received.	TenderNed.nl
priceratio	Percentage weight allocated to price in tender evaluation.	TenderNed.nl
length	Number of years of municipal audit contract.	TenderNed.nl
population	Total municipal inhabitants.	Statistics Netherlands
debt	Municipal net debt as percentage of total municipal income.	Ministry of the Interior and Kingdom Relations
distance	Distance in kilometres between municipal auditee's main LG office and office of appointed audit firm as mentioned in contract award notice.	Google Maps

Table 7: *Summary statistics dataset Dutch municipal auditor procurements, 2015-2020*

Variable	N	Mean	s.d	Min	Max
nonbig4	91	0.60	0.49	0	1
tenders	91	2.27	1.04	1	5
priceratio	91	32.10	10.18	0	70
length	91	3.20	0.92	1	6
population	91	68,586	62,269	10,246	360,000
debt	91	64.21	37.46	0	177.40
distance	91	76.73	59.90	0.55	258

Table 8: *Logistic regression results. Dependent variable non Big-4 auditor*

nonbig	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
tenders	-.484	.185	-2.62	.009	-.846	-.122	***
price	.027	.015	1.71	.087	-.004	.057	*
length	-.097	.175	-0.56	.579	-.439	.245	
population	0	0	-1.27	.205	0	0	
netdebt	-.001	.004	-0.20	.84	-.009	.008	
distance	-.004	.003	-1.32	.187	-.01	.002	
Constant	.472	.885	0.53	.594	-1.262	2.206	
Mean dependent var		0.253	SD dependent var			0.437	
Pseudo r-squared		0.161	Number of obs			91.000	
Chi-square		16.562	Prob > chi2			0.011	
Akaike crit. (AIC)		100.329	Bayesian crit. (BIC)			117.905	

*** $p < .01$, ** $p < .05$, * $p < .1$

Table 9: Overview findings country comparative analysis

	<i>England</i>	<i>The Netherlands</i>
Power of suppliers	Moderate – special registration requirements apply for auditors of LGs, however perceived to be a moderate barrier.	Low – no special statutory registration requirements for auditors of LGs.
Barriers to entry	Strong – minimum audit firm size requirement is a substantial barrier due to applied national procurement model.	Moderate – formal barriers low, although market perceived as complex and difficult to operate in successfully.
Power of buyers	Strong – however weakening as entry barriers are high and market interest is reducing given continuing reduction in audit fees.	Weak – however strengthening as entry barriers are limited and recent rise in audit fees is making market commercially interesting again.
Threat of substitutes	Low – little appetite for developing alternatives to private sector provision of audit services.	Moderate – some LGs are considering setting up their own (collaborative) audit organisation (following existing examples).
Rivalry	Strong – however declining market interest due to reducing fees and high entrance barriers.	Moderate – however growing due to entrance by small firms and renewed interest by some larger firms following recent rise in audit fees.

Figure 1: Porter's five forces that shape industry competition



Source: Porter (2008)