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Talk by Richard Murphy for the AGM conference

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When Prem Sikka first asked me to give this talk we agreed on a working title of “the games that accountants play”. I doubt that either of us realised how much material I’d be presented with in the meantime.

But there are quite a lot of things you don’t realise when they happen. I did not imagine when I worked for Peat Marwick, now KPMG, that I would describe them in the way I will today. But all the signs were there then.

Nor did I think in 1989 when I first wrote about the problems that pension funds would face as a result of their over investment in shares that the problem would be come generally apparent until about 2015, by when I thought it would be unavoidable. But we know it’s hit us now.
All three of these observations suggest two things. The first thing is that the glaringly obvious is usually staring us in the face, but very few see it, my colleagues here today excepted. The second is that the implications almost always arrive sooner than we expect.

It is of course glaringly obvious that there are just four large firms of accountants left in the world. My concern is that this has still not provoked a suitable response given the speed with which this situation has arisen. So far the most radical reaction has been from Sir Howard Davies of the FSA who said less than a fortnight ago that it is “now impossible for any of the remaining four to fail”. But the best action that he can recommend in consequence is that this matter be referred to the competition commission, the very authority that let the last two mergers of these firms happen.

Well, I don’t think that response is good enough. Let’s just suppose that we have another major corporate failure soon and the auditors are implicated. Suppose the auditors are one of the Big 4. Now I know it stretches credibility that this might happen, but let’s just suppose it did for a moment. What then? Is Howard Davies really
saying that whichever Big 4 auditor commits whatever audit error in the future the government must bail them out?

Let’s think about this for a minute. Andersen failed because of a US audit failure, but the UK firm buckled anyway. So is it now the case that the UK government thinks it will have no choice but bail out these firms wherever they fail? Did Howard Davies really mean that?

Or is he suggesting that the government now write unlimited professional indemnity insurance cover for these firms? If so, does he really think that removing their risk is going to increase the quality of their auditing? I hope not.

And what is he suggesting should happen if the UK firm that fails does so not because it did a bad audit but because of loss of confidence in the worldwide brand with which it was associated, which was what really killed Andersen UK? Is Howard Davies saying we still have to support it in that case, even though no one wants it any more?

I note that Gordon Borrie has rightly criticised some in the accounting profession for knee jerk reactions to some of
the recent proposals on audit reform. But I think he might also have criticised Howard Davies and others who have suggested that there is no alternative now but to shore up these firms, come what may. Because before this is seriously considered we need to ask some questions about the games that these firms play.

First of all we need to know just who we are talking about. You might think it’s PWC, KPMG, Ernst and Young and Deloittes. That’s because they are brand names as familiar in the auditing world as IBM, Microsoft, and Hewlett Packard are in the world of IT. Except these firms are not what they seem. IBM and so on are single world wide corporate entities. But the Big 4 auditors aren’t. They are all, at best, loose associations of national firms who make very clear that there are strong legal boundaries that separate them. For example Deloittes says it “delivers world-class services through its national practices”. And KPMG says it has a “global approach to service delivery” but then makes clear that this is done through its “member firms” and that “KPMG International is a Swiss non-operating association”. Variations on these themes are found at Ernst and Young and PWC.
In other words there aren’t four large auditors left in the world. There are in fact no large auditors in the world. What we actually have is a scattered selection of firms operating largely independently in about 150 countries in four loose associations.

The myth of the “Big 4” is not true. These firms propagate a lie that they are global players only when it suits them, which is when they’re looking for business. When it comes to avoiding liability, paying tax, or being accountable then the global image evaporates instantly and the legal substance comes to the fore. It’s worrying that Howard Davies, the senior regulator of the financial services industry in the UK, has bought the marketing lie. Like others he’s been tricked into believing what is just not true.

Why do these firms play this trick? Why does it suit them not to be global? There are two related reasons. By operating nationally and having only loose international links they can claim, as the UK partners of Andersen have, that they are not liable for what happens in the US. Of course, from Howard Davies’ point of view that might be good news as liability ends at the national boundary. But he should note that it didn’t save Andersen. And it has meant that those whom Andersen has harmed have less
recourse against the firm than they expected. For someone charged with protecting the consumer that doesn’t look such a good outcome after all.

Which is, of course, what the firms intend. They don’t want to be responsible to anyone if they can avoid it. By operating nationally they have a reduced duty of care.

And that’s particularly true with regard to tax. This issue is just as important as the first, and as worrying. I’m deeply concerned that the UK government might see itself as dependent upon the Big 4 firms. The reason is that those firms do not see themselves as having a responsibility to match any such dependency, if it exists.

If these firms really accepted the status they are being afforded you would expect them to act in appropriate fashion. One such indication might be that they published accounts even though until recently not required to by law. Good practice has suggested they should have done since the mid 1970’s. But PWC does not publish its UK results, nor even a summary of them. KPMG does publish UK results, but it’s a token gesture. The US firm of KPMG does not, and nor does the global firm. The other firms take broadly similar views.
Extraordinarily, at a time when it is becoming increasingly obvious that principle must be the basis of good accounting and that rule compliance is bound to lead to failure these firms have relied on the rules and denied principle. One has to question their fitness to regulate if they can’t show that they both understand and comply with the principles that must now govern the corporate world.

What they show by their contempt is that they do not recognise the rights of stakeholders, and of the government as a stakeholder in particular. It is admittedly incredibly difficult to find out what these firms think. But in my searches of the mission statements of these firms I have not found the concept of the stakeholder to be of concern to any but KPMG. All the rest focus only on themselves and their clients. Deloittes summarise this best by claiming their mission is “To help our clients and our people excel”. Ernst & Young are more verbose to say much the same. PWC manage to put their profit first.

But even KPMG cannot rest on their laurels. Although in their UK corporate report they have a stakeholder report, and in its preamble they recognise that the government
holds such status, they do conveniently neglect to report on their success in fulfilling their duty to the UK government. Perhaps this is just as well because KPMG is by far the largest off shore tax haven accountant in the world. Data I provided to the Guardian and which was published two weeks ago shows that it operates in 24 of the 32 states that the OECD recognises as having operated unacceptable taxation policies.

Less well known, but as importantly, it also operates in four of the seven states that are refusing to cooperate with the OECD in improving their tax practices. No one else operates in more than two. Despite this they are showing no sign of pulling out of them in consequence.

What does this say about KPMG? Quite clearly that it sees one of its principal objectives as being the promotion of tax avoidance. Since almost all the territories about which the OECD is concerned are tiny it also says that KPMG believe that it is quite acceptable for the corporate entity to avoid taxation by passing that burden to the populations of the nation states whose taxation income is reduced as a result. That includes the UK. It is also bound to include the governments of all the richer populous
countries of the world and those of all the populous lower income nations.

So whatever KPMG might say about its duty to the UK community in its stakeholder report it is actually through its actions saying something quite different. It is actually saying that it seeks to diminish the resources available for the public works required by that community by diverting those resources offshore through promotion of tax haven abuse.

And I want to make clear that’s just what they do. As example I’d suggest you look at the web site of KPMG Vanuatu, a full member of KPMG International. (http://www.kpmg.com.vu/) As you can’t do so at the moment I’ll give you some idea of what it says. On the home page it proudly states:

“Vanuatu is the longest established offshore centre in the Pacific. The legislation covering the various offshore vehicles is particularly user friendly and combined with its tax haven status and strict secrecy provisions, Vanuatu offers the perfect environment for carrying on offshore business at competitive prices.”
It then offers any willing punter the chance to set up an international company, bank account and trust to hide its ownership for just US$1,990. I stress, this isn’t in the small print. This is on the home page.

That home page goes on to proudly proclaim that KPMG is the only one of the Big 5 who operate in Vanuatu. They seem not to have noticed the world’s moved on although the page is dated June 2002. They also list the “practical and enticing” advantages of Vanuatu as a place to do business. High on this list is the fact that:

“Vanuatu has no personal or corporate income taxes, nor are there any withholding taxes, capital gains taxes, gift, estate or death duties for residents or non-residents. No tax treaties with other countries are in existence.”

This last fact is not surprising. KPMG fail to mention its not only on the OECD black list of tax haven abusers, it’s also refused to co-operate with the OECD in doing anything about that. But still KPMG encourages the world at large to use its services in this pariah state.

Just in case you’re not familiar with some of the facts that KPMG don’t tell you about Vanuatu the CIA Fact Book for
2001 (the only useful thing to come out of that organisation that I know of) adds the following:

- a majority of the population does not have access to a clean and reliable supply of water

- Vanuatu is a Y-shaped chain of some 80 islands, several of the islands have active volcanoes

- life expectancy is 60.95 years

- adult literacy is 53%

- The economy is based primarily on subsistence which provides a living for 65% of the population.

I’d love to know what proportion of the subsistence farmers KPMG prepares accounts for. I’d also be interested in what KPMG is doing for the community in Vanuatu. There seems a lot to do. But I somehow can’t imagine the KPMG Vanuatu stakeholder report is going to be published in the near future.

What other questions does this lead one to ask? I suggest the following:
• Is this a firm we want to regulate the corporate world?

• Or is this a firm that is leading corporate abuse of the nation state?

• Is this a firm that can regulate global capitalism?

• Or is it a group of national minnows with no clout against the global might of its clients?

• Is this a firm whose words we can trust?

• Or is this a firm who publishes statement that are inconsistent with its actions?

• Is this a firm who is objective when a corporate entity seeks to inflate bottom line profits?

  1. Or is this a firm that goes out of its way to encourage firms to do just that?

  2. Is this a firm with a clearly founded ethic of duty to the community?
• Or is it one that has an ethic based solely on self-interest?

• And is this a firm whose liabilities we want to underwrite at our own expense?

I know where I stand.

And I know what KPMG will say. They’ll suggest that what other member firms of KPMG International might do is not their business. But before accepting that we should note that the chair of KPMG International just happens to be the chair of KPMG UK. In which case, I suggest, there’s no real dividing line. If KPMG International is willing to operate in states such as Vanuatu, which has chosen to ignore the OECD tax haven guidelines and where their presence is clearly only required to service the tax avoidance industry (as KPMG’s local web site makes abundantly clear) then KPMG UK provides its explicit approval through the person of Mike Rake, its UK and worldwide chairman.

I’ll be quite specific. KPMG and the other large firms are playing games, right before our eyes. Yet it seems that even Howard Davies can’t see that. These firms aren’t
what they claim to be. They’re not global players. They’re not regulating global capitalism.

But they are undermining the governments of the world in pursuit of self interest. And they’re doing little else.

I think the conduct of these firms is unacceptable. I also think it is fundamentally undemocratic. Anyone who adopts a structure that is designed to subvert government income and does so in a way that reduces the chance of effective government enquiry into that action is, in my opinion acting unethically. The charge can therefore be laid at the door of all the Big 4.

So why are we now being asked to effectively underwrite their future? I know we’ve done this in the past by granting them a monopoly licence on auditing, as Prem Sikka and Austin Mitchell have pointed out. But now we’re looking at doing so again by granting them such a licence with the guarantee that they cannot loose. The partners must be laughing all the way to the bank.

But I don’t think this can last for long. Governments can’t protect the unsustainable for long. We should not live with these firms for much longer. I urge Howard Davies to have
the courage to both see that and put into action the necessary steps that must follow the demise of the next Big 4 firm, which demise is inevitable. That step cannot be to grant them immunity from failure. It is instead time to plan for a world when governments must act together to replace these firms with a new system of government co-ordinated regulation of global capitalism to assist the elimination of tax abuse, to protect investors and to protect stakeholders.

It is surely glaringly obvious that we now have no choice but do this, and that Howard Davies’ no choice option is bound to fail. I hope it’s not too late before he sees things that way.

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