

## **Invitation to Tender (ITT)**

### **Provision of Research Services**

### **Innovation and Competition in the Audit Market**

Reference	<b>FRC2022-0146 Research Services - Innovation and Competition in the Audit Market</b>
Date	<b>29<sup>th</sup> June 2022</b>

# Innovation and Competition in the Audit Market

## 1 Background and context

### *About the FRC*

The Financial Reporting Council (FRC) regulates auditors, accountants, and actuaries; and sets the UK's Corporate Governance and Stewardship Codes. We seek to promote transparency and integrity in business; our work is aimed at investors and others who rely on company accounts, audit, and high-quality risk management.

As the Competent Authority for audit in the UK, the FRC sets auditing and ethical standards, and monitors and enforces audit quality. The FRC will be transformed into a new regulator: the Audit, Reporting and Governance Authority (ARGA) in the future, following three independent reviews and recommendations, and the Government's 2021 consultation "Restoring trust in audit and corporate governance"<sup>1</sup> and the Government's response to that consultation.<sup>2</sup>

### *About the research project*

#### Purpose and scope

The aim of this research project is to further our understanding of how innovation and competition interact in the market for audit services. The FRC's strategic objectives for 2022-25 include promoting improvements and innovation in the areas for which we are responsible and creating a more resilient audit market through greater competition and choice.<sup>3</sup> The outputs of this research project will inform the FRC's work to drive up audit quality and improve the functioning of the audit market.

The theoretical literature on innovation and competition discusses the variety of the incentives at play. Broadly speaking, in well-functioning markets, competitive pressures encourage innovation. High rates of innovation can be an indicator of strong competition and can lead to improvements in the quality of goods and services offered to customers; innovation may also help the innovator to gain market power and profits. Both innovation and competition can contribute to increased productivity and economic growth.

The research project should build on earlier work by the Competition Commission<sup>4</sup> in relation to innovation in the audit market. It should also draw on wider understanding and experiences of innovation and competition, including that in sectors whose regulators also have innovation and competition objectives.

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<sup>1</sup> BEIS consultation on the government's proposals, [Restoring trust in audit and corporate governance](#), March 2021. This followed reviews by Sir John Kingman (2018), the CMA (2019) and Sir Donald Brydon (2019).

<sup>2</sup> Government response [Restoring trust in audit and corporate governance: Government response to the consultation on strengthening the UK's audit, corporate reporting and corporate governance systems](#)

<sup>3</sup> See [FRC 3 Year Plan 2022-25](#)

<sup>4</sup> Competition Commission, [Statutory audit services for large companies market investigation](#), October 2013 [Statutory audit services market investigation: final report \(publishing.service.gov.uk\)](#)

### Previous work on competition and innovation in audit

The evidence of the lack of competition in the audit market is well established. The Competition and Markets Authority (CMA)'s market study found that competition in the FTSE 350 audit market was insufficient and that there were no signs of the market self-correcting without further intervention.<sup>5</sup>

Some work has already been undertaken to examine innovation in the audit market. In 2013, the Competition Commission (CC), the CMA's predecessor, published its audit market investigation final report.<sup>6</sup> The CC examined innovation in some depth, in particular it considered: (a) constraints on innovation; (b) areas where innovation may be possible; (c) drivers of innovation; and (d) audit firms' views.

The CC reported audit firms had identified various areas of innovation with regard to the audit process. These ranged from a standardization of the audit approach and staff offshoring to greater automation, use of technology, and data analytics. The CC also noted audit firms identified areas of innovation in relation to enhanced auditor reporting to shareholders and management. The CC concluded that cost savings, operational efficiency gains and management of risk were the main drivers of innovation in audit. The CC also concluded that in a well-functioning market there would be scope for more innovation, for example, in response to shareholders seeking more information from audit.

More recently, the FRC has looked at the adoption of technology in audit, which is one form of innovation. This work, and a stakeholder consultation focused on the use of technology in audit, identified a number of barriers to technology adoption.<sup>7</sup> Staff training and skillset were identified as many respondents' (audit firms and professional bodies, as well as investors, third party technology providers and academics) primary concerns. Respondents also described significant challenges in accessing high-quality client data in a reliable and consistent format, meaning that the application of technological resources to improve audit quality can be practically challenging to deploy.

The importance of innovation in audit has also been highlighted more widely in the independent reviews of the audit market and its regulatory framework. The Kingman Review proposed that ARGA would consider, in relation to its competition objective, how competition between auditors could encourage innovation.<sup>8</sup> The Brydon Review considered how the audit

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<sup>5</sup> CMA, *Statutory audit services market study, Final Report*, April 2019  
[https://assets.publishing.service.gov.uk/media/5d03667d40f0b609ad3158c3/audit\\_final\\_report\\_02.pdf](https://assets.publishing.service.gov.uk/media/5d03667d40f0b609ad3158c3/audit_final_report_02.pdf)

<sup>6</sup> Competition Commission, *Statutory audit services for large companies market investigation*, October 2013  
[Statutory audit services market investigation: final report \(publishing.service.gov.uk\)](https://assets.publishing.service.gov.uk/media/5d03667d40f0b609ad3158c3/audit_final_report_02.pdf)

<sup>7</sup> FRC Discussion Paper (March 2020) Technological resources: using technology to enhance audit quality  
<https://www.frc.org.uk/getattachment/de3938e0-5e16-49f9-822b-b91f5bb844de/-.aspx>

FRC Response: [https://www.frc.org.uk/getattachment/352c4cc5-60a3-40d0-9f70-a402c5d32ab2/Technological-Resources-Using-Technology-To-Enhance-Audit-Quality\\_December-2020.pdf](https://www.frc.org.uk/getattachment/352c4cc5-60a3-40d0-9f70-a402c5d32ab2/Technological-Resources-Using-Technology-To-Enhance-Audit-Quality_December-2020.pdf)

<sup>8</sup> The Kingman Review, *Independent Review of the Financial Reporting Council*, December 2018  
[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/767387/frc-independent-review-final-report.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/767387/frc-independent-review-final-report.pdf)

sector could respond to the opportunities and challenges of new technology and other forms of innovation, both potentially playing a crucial role in increasing the effectiveness of audit.<sup>9</sup>

In addition, there is wider government interest in the role of regulators in relation to innovation and competition. The recent BEIS consultation on the UK regulatory framework considered whether every regulator should have a specific innovation and competition objective.<sup>10</sup> In the global context, international institutions and experts in competition policy emphasize the need for innovation-enabling competition policy as a means of fostering economic growth. This was also one of the key messages at a recent OECD competition conference.<sup>11</sup>

There remain significant gaps in evidence on links between innovation and competition in the audit market. There has been relatively little recent analysis on innovation as a driver of audit *quality* rather than/as well as a driver of cost efficiencies and risk mitigation. It is also unclear whether and, if so, under what circumstances, there could be potential trade-offs between innovation and competition.

## 2 Project description

### 2.1 Outputs and suggested approach

We envisage that the following outputs will be delivered by this research project:

- A short literature and (secondary) evidence review. This should include:
  - a summary of any research on the links between innovation and competition in the audit market. For this research project we are concerned predominantly with the audit market for FTSE 350 companies but would also be interested in innovation-competition dynamics in any other parts of the audit market for UK Public Interest Entities (PIEs) or in audit markets elsewhere in the world.
  - a summary of the latest research, both empirical and theoretical, on the interaction between innovation and competition at a more general level. This does not necessarily need to be audit specific providing findings could be of relevance to the audit market.
  - a summary of the available (secondary) evidence on innovations in audit since the previous work by the Competition Commission referenced above.
- Informed by the literature review and the evidence identified above, a short discussion paper with questions for discussion at the workshop (see below) with relevant innovation and competition experts. Potential research topics for discussion at the workshop are suggested further below. However, we will work with the appointed researcher to agree on the choice of potential topics and questions. The researcher

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<sup>9</sup> The Brydon Review, Assess, Assure and Inform: Improving Audit Quality and Effectiveness, Report of the Independent Review into the Quality and Effectiveness of Audit, December 2019  
[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/852960/brydon-review-final-report.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/852960/brydon-review-final-report.pdf)

<sup>10</sup> BEIS consultation, *Reforming the Framework for Better Regulation*, July 2021  
[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1005119/reforming-the-framework-for-better-regulation.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1005119/reforming-the-framework-for-better-regulation.pdf)

<sup>11</sup> OECD Competition Open Day February 2022 <https://www.oecd.org/competition/oecd-competition-open-day.htm>

will be also able to meet with FRC staff / audit experts to refine the paper and draw on internal FRC expertise.

- A small-scale structured (online) workshop with relevant innovation and competition experts from academia and other institutions such as think tanks and regulators (including the FRC). The aim of the workshop will be to share knowledge and insights, including those from other sectors of relevance (e.g. financial services / credit rating) that could be applied to the audit market. While knowledge of the audit market is desirable, we do not expect all workshop participants to be familiar with audit. Rather, we envisage that innovation / competition experts could bring their expertise and knowledge which could then be applied to the audit market. The expert workshop will be a core component of the project, and so the researcher will need to consider appropriate representation of participating experts.
- A short, written report, including the following:
  - (a) a summary of the discussion, insights, and findings from the expert workshop.
  - (b) any additional relevant insights and findings, potentially in the form of case studies, drawing on work from other regulators, both domestically and internationally.
  - (c) advice and guidance to inform ARGA's future work in promoting innovation while enhancing competition in the audit market. This should ideally include consideration of potential trade-offs and unintended consequences.
  - (d) suggestions on areas for further research on innovation in audit.

We welcome suggestions from bidders on the best approach to achieve the above outputs. Overall, this project is intended to bring together relevant experts in innovation and competition, in audit and in other relevant sectors such as financial services, to inform FRC policy in this area.

A similar type of research project (also including an expert workshop) has been recently undertaken by the Centre for Competition Policy at the University of East Anglia, commissioned by the Department for Business, Energy, and Industrial Strategy (BEIS).<sup>12</sup>

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<sup>12</sup> The research looked at innovation and competition in digital markets and informed the design and operational proposals for the new Digital Market Unit (competition regulator for digital markets). The research report and its findings were published alongside the BEIS consultation on the Digital Market Unit. Please see: [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1003985/uae-ccp-report\\_1\\_.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1003985/uae-ccp-report_1_.pdf)

## Potential themes and questions for evidence review and workshop discussion

We have identified three broad themes for this research project:

- **Theme 1: Understanding innovation in the audit market.** This could cover potential problems/barriers to innovation and opportunities, updating previous work e.g. by the Competition Commission, and providing the latest insights and evidence (where available). This could also include consideration of the definition and measurement of innovation in the audit market.
- **Theme 2: The relationship between innovation and competition in the audit market,** with a particular focus on how innovation could drive improvements in audit quality. This may also include the potential role of different firms, including challenger firms, in driving innovation.
- **Theme 3: Implications for ARGA's future policy and work in relation to innovation and competition,** drawing on recent work from other regulators for practical advice and recommendations. This could include consideration of the role that competition and regulatory policy and work could play in increasing innovation e.g. the use of pro-regulatory tools in boosting innovation such as sandbox initiatives etc.

These research themes are intended as guidance for prospective tenderers; they are not prescriptive. The project should be led by the expertise of the appointed researcher in discussion with the FRC research project panel. We welcome views and suggestions from the bidders on the formulation of the research themes and questions.

### 2.2 Liaison arrangements

The FRC team should be consulted on key decisions in the research design and its implementation. This will include regular project progress updates via Microsoft Teams and email.

### 2.3 High-level / indicative project timeline

***Please note that there is a degree of flexibility with respect to the start date for the project. However, we expect that the project will be fully concluded by March 2023.***

<i>Date</i>	<i>Deliverable / milestone</i>
w/c 19 September 2022 (indicative)	Project kick-off meeting (reviewing, and finalising research requirements; approach and scope of the project)
w/c 10 October 2022 (indicative)	Literature / evidence review
5 weeks before the workshop date (at the latest, earlier if possible)	Draft discussion paper ahead of the workshop / wider engagement with the experts
Within 2 weeks of the discussion paper submission	Draft reviewed by the FRC panel and comments submitted to the researcher
Can be undertaken in parallel with the activities above, starting soon after the project kick-off meeting	Preparation for the workshop with experts: format, scope, invitees etc.
TBC by the researcher, depending on the availability of experts	Workshop with experts in Autumn 2022 (November/December/January), depending on availability of experts.
Within 4 weeks following the workshop	Written draft report following discussion and analysis from the workshop
Following submission of the draft report	A meeting with the FRC project team to discuss emerging findings, this can take place online via MS Teams
Within 2 weeks following submission of draft report	Draft report reviewed by the FRC panel and comments submitted to the researcher
Within 2 weeks following FRC review	Final report submitted to the FRC panel

### 2.4 Cost and financials

The tenderer should provide a fixed fee for the work, exclusive of VAT, inclusive of all expenses. Tenderers should detail their costs in the Tender Response Documents in the format specified. No other costs should be charged on top of the fixed fee, unless the scope materially changes from what is set out / agreed. Changes to the scope / cost of the project must be mutually agreed.

***The FRC does not anticipate tender bids over £30,000 excluding VAT***

## 2.5 Your tender response

The proposal should be no more than 7 pages in total, excluding annexes, and include:

- A succinct summary of the proposal, including an estimated timeline of project milestones.
- Details of the proposed approach. This should include an overview of the review of literature and secondary evidence, as well as a high-level explanation of how you will access the appropriate expert networks in the field of innovation and competition to identify and attract suitable workshop participants.
- Your and your team's experience of similar projects and relevant research capability. The researcher should be familiar with the audit market to ensure appropriate evidence gathering and relevant findings.
- The arrangements to be put in place for managing this work and quality assuring outputs.
- A budget, including a breakdown of time and costs per activity, in line with the principal project objectives outlined above.
- Details of personnel to be involved, including their role for this project and their relevant experience.
- CVs for the project team should also be included in an annex, along with any additional information about your organization that you consider relevant.
- Bids should identify any real or perceived conflicts of interest.

## 2.6 Tender evaluation

Bids will be assessed against the following principal criteria:

- 25%: Understanding of our requirement (supported by relevant experience, track record and / or transferrable knowledge).
- 25%: The suitability of the approach (including methodology and management).
- 30%: Experience / relevant experience of the proposed personnel and evidence of existing networks and relations with the experts that would be beneficial to the project and potential participation in an expert workshop.
- 20%: Pricing / value for money of your proposal.

## 3 **References**

The FRC reserves the right to take up references. You will be required to provide references in the Tender Response Document. References must be relevant to the FRC requirement and in the last five years



#### 4 Use of ITT & publication

Tenderers **must not** undertake any publicity activity regarding the procurement within any section of the media.

#### 5 Questions & Clarifications

Tenderers may raise questions or seek clarification regarding any aspect of this tender at any time prior to the tender clarification deadline.

Tenderers may raise questions or seek clarification within the timeframe by sending questions to [procurement@frc.org.uk](mailto:procurement@frc.org.uk) in the following format.

Nature of query / clarification	Query / Clarification

The FRC will not enter into exclusive discussions regarding the requirements of this ITT with tenderers.

To ensure that all tenderers have equal access to information regarding this tender opportunity, FRC will publish all its responses to questions raised by Tenderers on an anonymous basis.

Responses will be published in a questions and answers document to all Tenderers who have indicated that they wish to participate.

#### 6 Tender process timeline

DATE/TIME	ACTIVITY
29/06/2022	Publication of the Invitation to Tender
25/07/2022 by 5pm	Deadline to submit clarification questions
28/07/2022 by 5pm	Deadline for publication of responses to clarification questions The FRC will endeavour to meet this deadline
05/09/2022 by 5pm	Deadline for supplier submission of tender to the FRC.

## 7 Conduct

The tenderer must not communicate to any person the tender price, even approximately, before the date of the contract award other than to obtain, in strict confidence, a price for insurance required to submit the tender.

The tenderer must not try to obtain any information about any other person's tender or proposed tender before the date of the contract award.

The tenderer must not make any arrangements with any other person about whether or not they should tender, or about their tender price.

The tenderer must not offer any incentive to any member of FRC's staff for doing or refraining from doing any act in relation to the tender.

If the tenderer engages in any of the activities set out in this section or if the FRC considers the tenderer's behaviour is in any way unethical, the FRC reserves the right to disqualify the tenderer from the procurement.

The tenderer represents and warrants that a conflicts of interest check has been carried out, and that check revealed no conflicts of interest.

Where a conflict of interest exists or arises or may exist or arise during the procurement process or following contract award the tenderer must inform the FRC and submit proposals to avoid such conflicts.

Tenderers must obtain for themselves at their own responsibility and expense all information necessary for the preparation of tenders. The FRC is not liable for any costs incurred by the tenderer as a result of the tendering procedure. Any work undertaken by the tenderer prior to the award of contract is a matter solely for the tenderer's own commercial judgement.

## 8 Due Diligence

While reasonable care has been taken in preparing the information in this ITT and any supporting documents, the information within the documents does not purport to be exhaustive nor has it been independently verified.

Neither the FRC, nor its representatives, employees, agents or advisers:

- makes any representation or warranty, express or implied, as to the accuracy, reasonableness or completeness of the ITT and supporting documents; or
- accepts any responsibility for the adequacy, accuracy or completeness of the information contained in the ITT and supporting documents nor shall any of them be liable for any loss or damage, other than in respect of fraudulent misrepresentation, arising as a result of reliance on such information or any subsequent communication.

It is the tenderer's sole responsibility to undertake such investigations and take such advice, including professional advice, as it considers appropriate in order to make decisions regarding

the content of its tenders and in order to verify any information provided to it during the procurement process and to query any ambiguity, whether actual or potential.

It is a requirement that the successful supplier (i) comply with all applicable laws and regulations including, without limitation, the Bribery Act 2010, the Equality Act 2010 and the Modern Slavery Act 2015; and (ii) in addition to any contractual requirement(s), inform the FRC immediately upon becoming aware of any event (including actual or threatened court proceedings) which may impact upon the reputation of the FRC, whether or not connected with the Supplies and/or Services.

## **9 Submitting a Tender**

Tenderers must submit their tender response within the deadline to [procurement@frc.org.uk](mailto:procurement@frc.org.uk).

Where a Tender Response Template is provided, potential providers must align their tender response with that format.

A Tender must remain valid and capable of acceptance by the Authority for a period of 90 days following the Tender Submission Deadline. A Tender with a shorter validity period may be rejected.

## **10 Evaluation**

The FRC will award the contract on the basis of the tender which best meets the evaluation criteria aligned to the requirements.

## **11 Acceptance of Tender & Notification of Award**

The FRC reserves the right to amend, add to or withdraw all or any part of this ITT at any time during the procurement.

The FRC shall not be under any obligation to accept the lowest price tender or any tender and reserves the right to accept such portion or portions as it may decide, unless the tenderer includes a formal statement to the contrary in the tender. The FRC also reserves the right to award more than one contract to fulfil the requirement.

The tenderer will be notified of the outcome of the tender submission at the earliest possible time.

Where the procurement process is subject to EU public procurement directives, a minimum standstill period of 10 calendar days will apply between communicating the award decision electronically to tenderers and awarding the contract.

Nothing in the documentation provided by the FRC to the tenderer during this procurement or any communication between the tenderer and the FRC or the FRC's representatives, employees, agents or advisers shall be taken as constituting an offer to contract or a contract.

No tender will be deemed to have been formally accepted until the successful tenderer has received a formal contract award letter from the FRC.

## **12 Additional Information**

Please use the attached Tender Response Document for your reply.

The Terms and Conditions that will apply to this proposed Agreement are attached. **Suppliers should accept the T&C's with no material changes.**