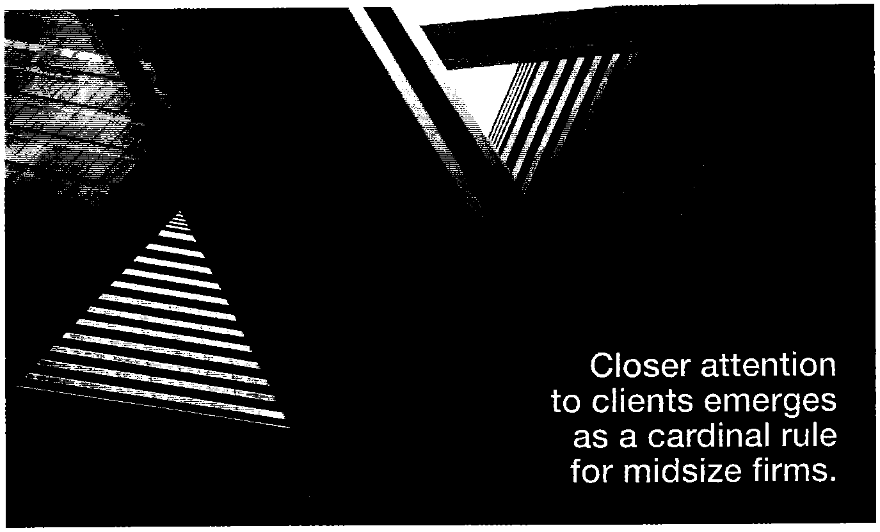
# Mid-Sized Accounting and Auditing Firms Target the Big Four




**By Charles W. Thurston**

Competition between midsize accounting and auditing firms and the Big Four is an ongoing struggle in which critical ground can be lost or gained daily. Investment consultant NEPC's 2015 survey on hedge fund operational due diligence indicated a general trend for hedge fund managers to move their business to the Big Four. Indeed, NEPC found that 23 percent of the 251 firms responding had changed service providers in the prior year.

In an effort to reverse the trend, some mid-market firms are probing their larger rivals for weaknesses. "Developing our consulting practice involved looking at the range of services available to Big Four clients and the needs of the market," says Michael Laveman, a tax partner at EisnerAmper. "We identified opportunities to support our clients with the issues—beyond tax and audit—that were of most value to them. It's how we have and continue to successfully build our firm: provide the expertise our clients want and need. That way, we can offer the same service as the Big Four yet can perform more nimbly. We may just be more user-friendly and still have more reasonable fees."

Marcum is another firm striving to distinguish its service from the Big Four's offerings. "The largest differentiators between us and the Big Four are personal service and price," says Beth Wiener, partner in charge of the Alternative Investment Group at Marcum. "We are able to provide excellent service at a more attractive price point and with professionals having many years of industry experience and in-depth knowledge of current accounting and regulatory requirements. We do this with a very personal approach and have few layers of red tape, so we are able to provide our services efficiently and expeditiously."

## Smaller clients demand more attention

Closer attention to clients emerges as a cardinal rule for midsize firms. "We have been meeting with a number of managers — both new launches and existing funds — that are actually looking for an alternative to the Big Four," says Alan Alzfan, partner and hedge fund practice leader at RSM. "Firms like RSM can provide the national and global expertise and resources of the larger firms but tend to provide more attention and personal service."

At Grant Thornton, "partner attention is a very big part of what differentiates us," says Michael Patanella, U.S. asset management sector leader. "Turnaround time for client questions, including technical ones, is at worst 24 hours. Some audit firms utilize the same procedures for public companies as for private funds. We have absolutely different procedures."

Size is also critically important to midsize firms. "RSM considers clients with only a few billion dollars of assets under management to be high-priority, and they receive a high level of attention, which they may not receive at a Big Four firm," says Alzfan.

## Harder-to-value investments

Communicating market value for clients that favor obscure financial structures is another special need, and an increasingly difficult demand for smaller service providers. "Hard-to-value investments are still a challenge from the auditor's perspective, as we must understand the valuation method and audit the key inputs and assumptions that go into the valuations. This information is not always easy to confirm and audit," says Alzfan. "We have developed separate valuation teams who are skilled in understanding these investments and the methods used to value them."

This trend is accelerating. "We have definitely seen an increase in harder-to-value securities over the past few years," says Wiener. "As funds are looking for differentiating opportunities, they are getting involved in more complex investment structures. Accounting standards have added more disclosure requirements to the financial statements as they relate to fair value, including details behind the unobservable inputs that a fund manager uses in their valuations. We have also seen more esoteric funds lately, such as those investing in art, Chinese porcelain or classic cars. Those pose their own set of challenges and usually involve the use of a third-party valuation firm."

## Regulation complicates fund distribution

Increasingly complex regulatory structures in more global markets means that midsize firms must ramp up their local representation and expertise if they want to compete with the Big Four. A survey by PricewaterhouseCoopers, released in December, found that the European Union's alternative investment funds Managers Directive (AIFMD) "has been a catalyst for firms to reconsider their distribution strategies — more than three quarters of managers in the survey say they have changed where or how they market non-EU alternative investment funds (AIFs) to EU investors in the wake of AIFMD."

One result of the growing worldwide regulatory burden has been consolidation among midsize accounting and audit firms. "[Dublin, Ireland-based] EisnerAmper Global was formed in October 2014 to provide solutions to clients that operate at a global level," says Nicholas Tsafos, an audit partner at EisnerAmper in New York, an independent member of the same global consortium. "You need to keep up with foreign regulations through the use of local talent and partners operating in those markets as well as with law firms that operate at a global level."

**Technology facilitates alternative investments**

Automating and analyzing alternative-investment data is a moving target for accounting and auditing firms, especially those not able to regularly invest tens of millions of dollars in new enterprise systems. But for many firms, it is essential.

"The adoption of technology into the auditing process has streamlined our procedures and allowed us to look at data in different, and often more useful, ways," says Wiener. "Accounts with a large number of transactions can be manipulated into formats that allow for detailed and efficient audit procedures. The use of sophisticated Excel formulas, macros and tables consolidates days of work into minutes. And they can bring our attention to anomalies that would be harder to detect manually."

Safeguarding against anomalies is especially important. "Audit analytics has allowed us to analyze large amounts of client data faster and in more detail," says Alzfan. "We have systems that look for unusual items based on certain parameters and then investigate those items. You can also compare information with other entities with a similar investment style and look for unusual trends in the financial data."

**Data security procedures deepen**

Cybersecurity requires that every accounting and auditing firm, regardless of size, maintain robust abilities and practices. "Data security is top-of-mind for our clients, our IT team, our partners and for our staff," says Wiener. "It is also paramount to the Securities and Exchange Commission, which is expecting registered investment advisers to implement cybersecurity programs. We continually work to enhance our security capabilities to keep up with the increasing risk of cyberthreats. In addition, we offer our clients an annually updated security posture summary highlighting our ongoing effort to secure their data, including encryption, advanced threat protection and regularly scheduled vulnerability assessments."

RSM's normal audit process includes documenting the controls and systems its clients have in place over all aspects of financial reporting, including elements of data security. "Our firm has a separate consulting practice, with one of their specialties being data and cybersecurity," says Alzfan. "As part of our conversations with our clients, we need to be discussing these issues, understanding the systems and procedures they have in place and making recommendations for best practices and improvements. Our consulting practice can help our clients in designing systems, penetration testing and responding to a breach of their systems."

Helping clients balance cybersecurity risk and resources is often part of the brief as well. "A lot of firms go for security implementation and deployment," Patanella notes. "We prefer to sit beside the chief technology officer and advise them on new risks, on how to prevent breaches and how to make sure they are utilizing every dollar in the best area."

Accompanying their efforts both to match the Big Four's capabilities and to provide unique services, however, some midsize firms believe they can offer a further differentiator: stability. At Grant Thornton, "among the reasons that we continue to see clients come in from the Big Four is that a good number of managers are not happy with their high turnover, with their not competing on audit work for private equity, nor with their high prices," says Patanella. "The average turnover with the Big Four can be as high as 30 percent per year. We're now under 10 percent." ■