



**Meeting Location:** Conrad Hotel, Dublin, Ireland

**Meeting Date:** February 20-22, 2012

## Regulatory Developments

### Objective of Agenda Item

To receive an update on developments regarding EC proposals for a Regulation on specific requirements regarding the statutory audit of public-interest entities.

### Proposed EC Regulation

In October 2010, the European Commission issued a green paper entitled “Audit Policy: Lessons from the Crisis”. The paper noted that the Commission would like to open a debate on the role of the auditor, the governance and independence of audit firms, the supervision of auditors, the configuration of the audit market, the creation of a single market for the provision of audit services, the simplification of rules for Small and Medium Sized Enterprises (SMEs) and Practitioners (SMPs) and the international co-operation for the supervision of global audit networks. IESBA submitted comments on relevant matters. An update was provided at the October 2011 IESBA meeting in New York.

In December 2011 the EC issued proposals for a Directive amending the Directive on statutory annual accounts and consolidated accounts, and also proposals for a Regulation on specific requirements regarding the statutory audit of public-interest entities.<sup>1</sup> In particular, within Title II, Chapter 1 of the proposed Regulation covers Independence and avoidance of conflict of interest. The Explanatory Memorandum accompanying the proposal states, in relation to Chapter 1:

“An auditor should establish adequate policies and procedures to ensure compliance with the obligations under the Regulation regarding independence, internal quality control systems and the supervision of employees.

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<sup>1</sup> The main legal acts of the EU come in three forms: [regulations](#), [directives](#), and [decisions](#). Regulations become law in all member states the moment they come into force, without the requirement for any implementing measures, and automatically override conflicting domestic provisions. Directives require member states to achieve a certain result while leaving them discretion as to how to achieve the result. The details of how they are to be implemented are left to member states.

Former auditors, key audit partners or their employees are not allowed to take up a key management position in the audited entity, to become a member of the audit committee of the audited entity, to become a non-executive member of the administrative body or to join the supervisory body of the audited entity within two years after the termination of the audit engagement.

The fees for the provision of related financial audit services to the audited entity should be limited to 10 % of the audit fees paid by that entity. Additionally, where the total fees, audit and related financial audit services, received by an auditor from a PIE reach a significant percentage of his/her/its total annual fees, appropriate safeguards should be applied.

The statutory auditor, audit firm or member of the audit firm's network will be prevented from providing certain non-audit services which are fundamentally incompatible with the independent public-interest function of audit to their audited entities in all cases, while for other non-services that are not fundamentally incompatible with the audit services, the audit committee or the competent authority will be empowered to assess, depending on the concrete circumstances, whether or not they may be provided to the audited entity. However, related financial audit services could be provided. The Commission is empowered to adapt the lists of authorised services and of prohibited services in accordance with the conditions set out in Title VI. In addition, audit firms of significant dimension should focus their professional activity on the carrying out of statutory audit and should not be allowed to undertake non-audit services.

Before accepting or continuing an engagement, an auditor should assess all potential threats to his/her/its independence and confirm his/her independence to the audit committee.”

Chapter 2 covers Confidentiality.

Title III covers the appointment of statutory auditors and regarding auditor rotation, the Explanatory Memorandum states:

“With a view to addressing the threat of familiarity that results from the audited undertaking often appointing and re-appointing the same audit firm for decades, the regulation introduces mandatory rotation of audit firms after a maximum period of 6 years that may be, under certain exceptional circumstances, extended to 8 years. Where a public-interest entity has appointed two or more statutory auditors or audit firms, the maximum duration of the engagements will be 9 years; on an exceptional basis, such duration may be extended to 12 years. It also provides for a cooling-off period before the audit firm is able to carry out the statutory audit of the same entity again. In order to ensure a smooth transition the former auditor is required to transfer a handover file with relevant information to the incoming auditor.”

This video link provides a 7 minute Technical Briefing by Claire Bury, Acting Director “Capital and Companies” followed by Q&A:

[http://ec.europa.eu/internal\\_market/auditing/reform/index\\_en.htm](http://ec.europa.eu/internal_market/auditing/reform/index_en.htm)

**Action Requested**

IESBA members will be provided with an update on developments on EC proposals for a Regulation on specific requirements regarding the statutory audit of public-interest entities.

**Material Presented**

Agenda Paper 9

Agenda Paper 9-A

This Agenda Paper

Proposal for a Regulation of the European Parliament and of the Council on specific requirements regarding statutory audit of public-interest entities.

**Action Requested**

1. IESBA members will be provided with an update on developments.