

25 February 2011

Green Paper on Audit Policy 'Lessons from the Crisis'

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IAASB CAG meeting 8 March 2011

- I. Context
- II. Scope of the Green Paper (GP)
- III. Feedback Statement
- IV. Next Steps

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I. Context

- The Green Paper is a ***consultation*** document.
- It identifies the issues and consults on how best to address them.
- There are ***no formal*** Commission ***proposals*** at this stage.

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II. Scope of the Green Paper

1. Role of the auditor
2. Governance and independence
3. Supervision
4. Audit market
5. A European Passport for auditors?
6. Simplification SMEs and SMPs
7. International co-operation and supervision

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II.1. Role of the Auditor

- some of the questions raised in the GP

- What improvements to the audit report should be explored?
- Should communication between auditors and external stakeholders be improved?
- Should communication with the Audit Committee be improved?
- *When and how should ISAs be introduced at EU level?* Binding instrument? Recommendation?

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II.2. Governance and Independence

– Some of the questions raised in the GP

- Is there a **conflict of interest** in the nomination procedure of the auditor?
- Should **rotation** of partners and firms be mandatory?
- Should **non-audit services** be further restricted? Prohibited?
- Should the **ownership rules** of audit firms and the partnership model be revisited?
- Should there be limitations on share of fees a single client represent for a firm?

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II.3 + II.5. EU Supervision and passport

- Some of the questions raised in the GP

- How can EU oversight be further strengthened?
- Is there a need for a European Passport for auditors combined with a maximum harmonisation of professional qualifications, governance, ownership and independence rules?
- Should this also mean European supervision (CRA model)?

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II.4. Audit Market

- some of the questions raised in the GP

- Could concentration in the listed companies audit market (more than 90% Big 4) entail systemic risk?
- Potential structural solutions for discussion:
 - Joint audits?
 - Mandatory rotation/retendering?
 - Addressing the 'Big Four is best' bias?
 - Contingency plans for a "systemic" firm?
 - Reassessment of the drivers of past consolidation?

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II.6. Simplification SMEs and SMPs

- Some of the questions raised in the GP

- Need to calibrate any proposals the Commission will adopt as a follow-up to the Green Paper.
- SMEs have fewer stakeholders and are usually owner managed.
 - Do we need to audit SME financial statements?
 - Would a 'lighter audit' be sufficient to provide comfort to creditors, lenders and the tax authorities?
- Do SMPs require less stringent quality control and supervision?

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II.7. International Co-operation and Supervision

- International cooperation is **key**
 - Discussions should take place at FSB and G20 level
 - The supervision of large global audit networks is a matter of concern. What measures should be adopted at a global level for the supervision of group audits and global audit networks?

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III. Feedback Statement regarding ISAs

Profession

- Professional bodies: support binding adoption (but some suggested room for modifications)
- Audit firms: broad support for binding adoption without further adaptation for SMEs and SMPs
- SMPs: request sensitivity to additional administrative burden

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III. Feedback Statement regarding ISAs

Investors

- support application of consistent **global** standards (not limited to EU)
- Most investors: flexible, non-binding approach (fit for purpose)
- Some investors ask for review of IAASB governance to include more investors in development ISAs

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III. Feedback Statement regarding ISAs

Public Authorities

- broad support though not always via binding measures
- CESR, CEIOPS and CEBS support binding adoption
- EU oversight authorities have no consensus on add-ons/carve outs

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III. Feedback Statement regarding ISAs

Academics

- support for binding standards.
- Warning for the risk of non-application of ISAs by US (would render ISA not fully global standards)

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III. Feedback Statement

regarding ISAs

Companies

- Less enthusiasm for ISAs though no opposition provided reservations are addressed, such as:
 - Reinforce governance and due process of IAASB (too accountant/auditor dominated)
 - Specific assessment and adoption approach in EU (different from IFRS)
- Regarding SMEs and SMPs, support to further explore but some concerns that ISAs should better suit SMEs and SMPs.

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III. Feedback Statement

- regarding appointment of auditors

Profession

- Limited support for third party involvement in nomination auditor in exceptional circumstances
- **Professional bodies**
 - Majority consider Code of Ethics and effective independent audit committees sufficient
- **Big 4**
 - No independence problems in particular in case of effective independent audit committees
- **Mid tier firms and SMPs**
 - Role of independent audit committees should be strengthened.
 - Avoid management having a role in the appointment

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III. Feedback Statement

- regarding appointment of auditors

Investors

- Conflict of interest inherent but can be mitigated
- Limited support for third party involvement in exceptional circumstances

Possible ways to solve potential conflicts of interest

- Shareholders should approve the auditor
- Independent audit committee
- Minimum standards on transparency regarding the relationship between the company and its auditor
- More transparency when changing auditors
- ...

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III. Feedback Statement

- regarding appointment of auditors

Public authorities

- Appointment and remuneration responsibility of independent audit committees
- Third party involvement possible but in limited cases of public interest

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III. Feedback Statement

- regarding rotation and tendering

- **Professional organisations** opposed to rotation but support (mandatory) tendering on regular basis with strong role for independent audit committee.
- **Big 4** oppose limitation of continuous engagement of audit firms.

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III. Feedback Statement

- regarding rotation and tendering

- **Mid Tier firms and SMPs** oppose mandatory rotation but show support for (non mandatory) tendering.
- **Investors** ask more transparency from companies and independent audit committees on appointment and possible retendering.

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III. Feedback Statement

- regarding rotation and tendering

- **Public authorities:** mixed views on mandatory rotation but broad support for mandatory re-tendering.
- **Academics:** some support (less risk of auditor wanting to accommodate company)

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III. Feedback Statement

- regarding rotation and tendering

- **Companies** do not support mandatory rotation but are generally in favour of retendering (with possibility to keep same audit firm if benefits of continuity are demonstrable).

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III. Feedback Statement

- regarding non-audit services

- Vast majority **professional organisations** opposed to any ban, only limited support in case of PIEs
- **Big 4** opposed to prohibition though some openness as regards non-audit services for audit clients
- **Big 4** support strengthening role of independent audit committees (approval)
- **Mid tier and SMP**: only in case of PIEs

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III. Feedback Statement

- regarding non-audit services

- **Investors:**
 - list of non-audit services that are allowed/prohibited
 - transparency on non-audit services provided by audit firm
 - strengthening role independent audit committees
- **Public authorities:** list of non-audit services and strengthening role independent audit committees

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III. Feedback Statement

- regarding non-audit services

■ **Academics:**

- broad support for full cessation of non-audit services or ban of non audit services for audit clients
- strengthening role independent audit committee;
- monitoring and transparency on violations;
- reference to SEC (not audit own work/not role management/not serve in advocacy role for client)

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III. Feedback Statement

- regarding non-audit services

- **Lawyers, tax advisors** opposed to auditors providing non-audit services
- **Companies** do not support EU wide prohibition of non-audit services (audit quality). Some suggest limiting it to non-audit services for audit clients

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IV. Next Steps

- Commission is reflecting on replies to GP and discussions held during the conference on 10 February 2011
- Commission proposal planned for November 2011

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These were my personal views

All replies that allowed publication are available on our website.

Summary of replies received by question and by stakeholder group available on our website:

[http://ec.europa.eu/internal_market/
consultations/2010/green_paper_audit_en.htm](http://ec.europa.eu/internal_market/consultations/2010/green_paper_audit_en.htm)

presentations (including speech Commissioner Barnier) made at the Conference on Auditing and video of the Conference available on our website:

[http://ec.europa.eu/internal_market/accounting/
conference_20110209_en.htm](http://ec.europa.eu/internal_market/accounting/conference_20110209_en.htm)

■ Thank you

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