

Meeting: IESBA CAG

Meeting Location: New York

Meeting Date: September 9-10, 2014

Agenda Item

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Long Association – Cover Note and Report-Back

Objectives of Agenda Item

1. To provide a report-back on proposals of CAG Representatives on this project as discussed at the June 2014 CAG Teleconference.
2. To advise CAG Representatives of the issuance of an exposure draft and to invite their organizations to comment on it.

Project Status and Timeline

3. The IESBA approved the project proposal at its December 2012 meeting. It has subsequently met to discuss the proposals in June and December 2013 and April and July 2014.
4. The main issues considered in the project are:
 - (a) Strengthening the general framework in the Code surrounding long association
 - (b) Communication with those charged with governance as it relates to partner rotation
 - (c) Time served on an audit before becoming a key audit partner
 - (d) Duration of the cooling-off period
 - (e) Permissible activities during cooling-off
5. The IESBA voted out an exposure draft at its July 2014 meeting (item D-1 below).

June 2014 CAG Discussion

6. Below are extracts from the draft minutes of the June 2014 CAG Teleconference, and an indication of how the project Task Force or IESBA has responded to CAG Representatives' comments.

Representatives' Comments	Task Force/IESBA Response
IS THE PROJECT STILL IMPORTANT TO CONTINUE?	
Mr. Fukushima indicated that, as noted in IOSCO's comment letter in response to the IESBA's Strategy and Work Plan consultation paper, he supported the IESBA undertaking this project because familiarity with an audit client	Support noted.

Representatives' Comments	Task Force/IESBA Response
can undermine an auditor's objectivity.	
Mr. Hansen confirmed that he supported the project because it was important, not only for the profession, but also in the public interest.	Support noted.
Ms. Hollein commented that her constituents support the continuance of the project. She emphasized the importance of considering what would be in the best interests of all stakeholders.	Support noted.
Noting that she represents the institutional investor view, Ms. Molyneux noted that the project was critical mostly because of the issue of perception. She commented that it was important for auditors to be seen to act independently. Mr. Waldron concurred.	Support noted.
SHOULD THE ENGAGEMENT QUALITY CONTROL REVIEW PARTNER (EQCR) BE SUBJECT TO THE SAME REQUIREMENTS AS THE ENGAGEMENT PARTNER?	
Mr. Hansen was of the view that the EQCR is at least as important as the engagement partner. He noted that the EQCR's involvement is the last step in the process before the audit report is signed and, accordingly, objectivity and independence are just as important to this role. He wondered what the approach for the EQCR would be if it were not the same as for the engagement partner, noting his concern that the EQCR could become the engagement partner and therefore be closely associated with the client for a longer period.	Point considered by the IESBA but ultimately not accepted by the majority. Ms. Orbea indicated that all key audit partner roles on an audit are important because they are making significant judgments that impact the outcome of the audit. She noted that under the current proposals, they would all continue to be subject to the existing rotation provisions of seven years on and two years off. She added that the intention was not to convey that the EQCR has a less important role. Rather, on the basis that the Code has appropriate provisions now, there is a need to address the concerns that have been raised by stakeholders and it is the engagement partner that is most subject to significant familiarity and self-interest threats. She noted that while the EQCR's review is important, he or she has less contact with the client and is therefore most independent from the audit team. Accordingly, the strengthened proposals would be better focused on the engagement partner.
Mr. Waldron agreed with Mr. Hansen, noting that audit inspection findings released by the PCAOB	See the response to Mr. Hansen's comment above and Ms. De Beer's comment below.

Representatives' Comments	Task Force/IESBA Response
<p>in the last six months had highlighted issues that should have been identified by the EQCR. He was of the view that because of their role, particularly on large audits, EQCRs should be subject to the same provisions as engagement partners. Accordingly, he felt that the proposals would be flawed if the EQCR is not subject to the same requirement as the engagement partner. He also commented that clients know and are familiar with EQCRs who work with engagement partners.</p>	
<p>Ms. Molyneux agreed with Messrs. Hansen and Waldron on the grounds that audits should be robust. While the engagement partner needs objectivity, she felt that this is really backed up by the EQCR. Accordingly, she felt that the two should be subject to the same requirements.</p>	<p>See response to Mr. Hansen's comment above.</p>
<p>Ms. de Beer noted that the EQCR plays a really important role even though he or she may not have the same level of interaction with the client. She felt that perception is important and therefore she supported a longer cooling-off period for the EQCR aligned with that for the engagement partner. Mr. Bluhm concurred with the views that both the engagement partner and the EQCR should be subject to the same requirements.</p>	<p>See response to Mr. Hansen's comment above. The IESBA has taken the importance of perception into account in its proposals and on balance concluded that the significance of the familiarity threats created by the long association of the EQCR with the audit client is less than created by the engagement partner's both in fact and appearance.</p>
<p>Mr. Fukushima indicated that IOSCO had not yet reached a consensus on this issue. He expressed a personal view that the EQCR should be subject to the same requirements as the engagement partner. He commented that in Japan the engagement partner and the EQCR have the same five-year time-on period. He noted that regardless of whether or not the EQCR is in contact with the client, the EQCR is involved in the sign off on the audit engagement and accordingly the EQCR's objectivity is as important as the engagement partner's.</p>	<p>The IESBA noted the lack of a consensus but will welcome comments from IOSCO on the exposure draft. For the IESBA's view on the EQCR's role see comments above.</p>
<p>Mr. Koktvedgaard invited Mr. Fukushima to</p>	<p>Noted.</p>

Representatives' Comments	Task Force/IESBA Response
<p>consider the issues further with his colleagues in IOSCO in order to have a consensus IOSCO view on the issue. Mr. Fukushima indicated that as the issues are complex it is difficult to reach a consensus but he agreed to confer further with his colleagues within IOSCO.</p>	
<p>Ms. Elliott indicated that if the IESBA is trying to address the perception issues, which are likely to be concentrated on the engagement partner, then the focus should be on the engagement partner. However, she acknowledged other views concerning the EQCR and indicated that she would support the majority. She nevertheless expressed a concern about the impact on resources, noting a preference for simplicity and avoiding imposing unnecessary restrictions.</p>	<p>Point noted.</p>
<p>Commenting in a personal capacity, Mr. Finnell indicated that the insurance industry only considers rotation of the engagement partner and not of the EQCR. He noted that in his experience, as time goes on it is less likely that the EQCR would work in the same office as the engagement partner. He highlighted the very important roles of individuals in the firms' national offices. He added that although the engagement partner and EQCR both have very important roles, generally the issue comes down to one of perception and not hard evidence. Accordingly, he expressed the view that the focus should be more on the engagement partner.</p>	<p>Support noted.</p>
<p>Ms. Hollein, (Ms. Manabat by email) and Mr. Thompson noted that the focus should be on the engagement partner as long as the perception issue is addressed. Mr. Thompson indicated that the roles of the engagement partner and the EQCR are distinctly different. The engagement partner makes the decisions on the audit, albeit in consultation with the EQCR. He noted that the public will only see the engagement partner as</p>	<p>Points noted and accepted.</p>

Representatives' Comments	Task Force/IESBA Response
the one who signs the audit report and therefore he considered that the perception concern lay only with the engagement partner.	
DURATION OF THE COOLING-OFF PERIOD	
Representatives (including Ms. Manabat via email) broadly expressed support for the cooling-off period for engagement partners being extended to five years without listed entities being distinguished from public interest entities (PIEs).	Support noted.
Ms. Elliott commented that the proposal gives a strong message to address the issue of perception	Point noted and accepted.
Mr. Bluhm, felt that a five-year cooling-off period is a concern within the small and medium practices (SMP) community. He added that it would be more helpful if the extension to the cooling-off period were limited to audits of listed entities.	Point noted, however in order to address perception concerns that had been raised, the IESBA considered that the current two-year cooling-off period for engagement partners should be extended and that a five-year cooling-off period was the preferred option for the extension of the cooling-off period. Three years was not seen as making any significant difference and four years was not a cooling-off period used in many jurisdictions and would lead to greater implementation challenges. The IESBA concluded that there was little justification for making any distinction between listed companies and other PIEs as they are all entities of public interest and are treated the same way in the Code.
PERMISSIBLE ACTIVITIES	
Mss. Molyneux, Hollein and Elliott, and Messrs. Finnell, Thompson and Waldron supported the proposals. Mss. Molyneux and Hollein commented that they allowed for proper cooling off, having regard to the need not to unduly restrict access to specialist resources, and were practical.	Support noted.
Mr. Thompson commented that the key principle was that the outgoing partner should not	Point accepted.

Representatives' Comments	Task Force/IESBA Response
influence the outcome of the audit during the cooling-off period.	
Mr. Hansen expressed general support for the proposals. He was of the view that it should only be on an exception basis that the outgoing engagement partner be consulted on the prior audit conclusions and that he or she should not have any influence on the conclusions on the current engagement.	Support noted and point accepted.
Mr. Fukushima, expressing a personal view, questioned whether after two years has elapsed, the exemption could be applied in a consistent manner because it may sometimes not be easy to distinguish the audit of transactions or events in which the engagement partner was previously involved from the audit of transactions or events in which the engagement partner was not.	Point noted and considered, however the IESBA concluded that the rotated engagement partner could be allowed to undertake a limited role after two years had elapsed, as the self-interest and familiarity threats would have diminished after two years of limited contact with the engagement team and the audit client. This approach would strike the balance between addressing threats to independence and enabling potentially limited resources and technical skills to be made available to safeguard audit quality.
Ms. de Beer expressed support for the proposals in principle but questioned whether, if an individual is cooling off the engagement, any manner of return should be allowed. She supported the proposed exception in respect of the consultation of industry specialists but did not think that non-audit services should be permitted during cooling off. Overall, she felt that the proposals were going in the right direction.	Support noted. Regarding non-audit services the IESBA took such feedback into account and considered that the proposed provisions in 290.150B strike the right balance in relation to non-audit services which are only able to be undertaken in restricted circumstances.

Matter for CAG Consideration

7. CAG Representatives are encouraged to invite their organizations to comment on the exposure draft.

Material Presented – CAG Paper

Agenda Item D-1 [Long Association Explanatory Memorandum with Exposure Draft.](#)