

Meeting: IESBA CAG

Meeting Location: New York

Meeting Date: September 14, 2015

Agenda Item

B

Long Association—Report-Back

Objectives of Agenda Item

1. To note the report-back on the March 2015 CAG discussion.
2. To obtain feedback from CAG Representatives on the Board's current proposals regarding the Code's long association provisions.

Project Status and Timeline

3. The IESBA voted out the Exposure Draft (ED), [Proposed Changes to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client](#), at its July 2014 meeting. The comment period closed on November 12, 2014. Comment letters were received from 77 respondents.
4. The IESBA considered summaries of significant comments on the ED at its [January](#) and [April](#) 2015 meetings. At these meetings, the IESBA considered, among other matters, options with regard to the cooling-off provisions for the Engagement Quality Control Reviewer (EQCR) and the Engagement Partner (EP); and whether the existence of different regulatory safeguards, or a package of safeguards, set at the jurisdictional level might provide an alternative to elements of the partner rotation requirements for audits of public interest entities (PIEs) in the Code.
5. This project was last considered by the CAG at its March 2015 meeting. Owing to the level of debate and time constraints, Representatives were able to provide input on only some of the issues that were presented. At this meeting, Representatives will be asked for their feedback on the remaining issues from the March 2015 meeting, and the current tentative conclusions that the Board has reached as a result of its deliberations at its April and June/July 2015 meetings.

March 2015 CAG Discussion

6. Below are extracts from the draft minutes of the March 2015 CAG meeting,¹ and an indication of how the project Task Force or IESBA has responded to Representatives' comments.

| Matters Raised | Task Force/IESBA Response |
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| LENGTH OF TIME-ON PERIOD FOR ALL KEY AUDIT PARTNERS (KAPs) | |
| CAG Representatives made no comments on | — |

¹ The March 2015 minutes will be approved at September 2015 CAG meeting.

| Matters Raised | Task Force/IESBA Response |
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| this proposal. | |
| LENGTH OF COOLING-OFF FOR EP | |
| Mr. Hansen supported the proposed five-year cooling-off period for the EP. | Support noted. |
| Ms. McGeachy expressed concern about the direction of the proposal given that the majority of respondents did not support a five-year cooling-off period. She believed that whilst the profession might be accused of self-interest, when such a large proportion of respondents have the same view, that view should not be discounted. She commented that the provisions had only recently been introduced and that she was not aware of any research indicating that the two-year cooling-off period was inadequate. She was of the view that mandatory firm rotation should be factored into the Board's assessment of the long association provisions. She added that global convergence is in the public interest and that the closer the world can reach the same provisions, the better it would be for the market. | Comments noted and taken into account in Board discussions. See the agenda papers and IESBA minutes. |
| Ms. de Beer noted that given that mandatory firm rotation was already in place in a number of jurisdictions around the world, this was a signal for the Board to strengthen the Code's provisions. | Comments noted and taken into account in the Board's discussions at its April and June/July 2015 meetings. |
| Ms. Robert supported Ms. McGeachy's comments on global convergence, noting that the Board should not undermine provisions that are already in place at the jurisdictional level to address long association. She highlighted, for example, the debate over many years in the EU that led to the recent mandatory firm rotation legislation. Given this context, she expressed a concern that in Europe the proposals in the ED would be very complex to implement and monitor. Accordingly, she was of the view that convergence would not be achievable with the current proposals. | See response to Ms. McGeachy above. |

| Matters Raised | Task Force/IESBA Response |
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| LENGTH OF COOLING-OFF FOR OTHER KAPs INCLUDING THE EQCR | |
| <p>Mr. Hansen indicated that he did not support the view that the EQCR should cool off for only two years because he regarded the EQCR as being involved in key decisions on an audit. He disagreed with the comments in the report-back, in particular that the EQCR is usually not known to, and has no contact with, the client, and that it would not be necessary to have another control on top of the EQCR's control role. He noted that in his experience the EQCR is usually known to the client and is involved in major decisions. He added that whilst the EQCR might not be the decision maker, the EQCR's involvement comes right at the end of an audit and he or she plays a key role at that time.</p> <p>Ms. Orbea indicated that the views of CAG Representatives on the June 2014 conference call had been quite evenly split on the cooling-off period for the EQCR. She explained that the same theme had come through from the comment letters. She emphasized that the Board was not viewing the roles of the EQCR and other KAPs as unimportant, because the Board acknowledged that these are roles that make significant judgments. She explained, however, that the Board was targeting the individual who was at the greatest risk of familiarity, i.e., the EP.</p> | <p>In light of the CAG discussion, the Board has now revised its package of proposals which it believes, taken as a whole, address the relevant issues. See Agenda Item B-1.</p> |
| <p>Mr. Waldron agreed with Mr. Hansen. He indicated that the CFA Institute regarded the EP and EQCR as so close and integral to the audit process that they should be treated the same. He noted that inspection reports from the PCAOB had flagged issues on audits that should have been identified by the EQCR, thus highlighting the importance of the EQCR role. He noted that IOSCO had expressed support for the EQCR being treated the same as the EP with respect to cooling off. He urged the Board to carefully consider the advice from the CAG and to have regard to the public who relies on</p> | <p>See response to Mr. Hansen above.</p> |

| Matters Raised | Task Force/IESBA Response |
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| audited financial statements. | |
| <p>Ms. de Beer agreed with Messrs. Hansen and Waldron, noting the need for care in considering who was raising comments on the ED. With respect to the ED proposal allowing for the rotated EP to undertake a limited consulting role with the engagement team or client after two of the five years in the cooling-off period have elapsed, she was of the view that this would dilute the provision. She felt that a better approach would be to impose a strict cooling-off with no involvement with the engagement team or client. Mr. Greene agreed with Mr. Hansen and Ms. de Beer on the EQCR issue.</p> | <p>See response to Mr. Hansen above.</p> |
| <p>Mr. Thompson agreed that the EQCR plays a very important role in the audit process. He noted that he had himself served in that role on a number of listed audits and that the clients never knew him. He considered that in Europe the client usually neither knows the identity of nor meets the EQCR. He noted that practices may differ in other jurisdictions. He was of the view that only the EP should be the key contact with the client. He suggested the need to distinguish among the roles of the various KAPs on an audit engagement and to address those roles separately, i.e., the EP who plays the most important</p> | <p>Comments taken into account by the Board. See the accompanying agenda papers.</p> |
| <p>Mr. Hansen commented that he knew of situations where clients had expressly requested that certain individuals not be appointed EQCR for their audits. He suggested that the Board might perhaps consider the merit of prohibiting contact between the EQCR and the audit client.</p> | <p>Ms. Orbea noted that the Board is very much aware of the source of comments on the ED. She explained that the Board had listened to concerns expressed by stakeholders about an individual being able to serve on an audit of a PIE for 14 out of 16 years. She noted that the Board had always come back to consider the perception of a lack of independence and considered that such a perception was at its greatest with the role of the EP. Ms. Orbea confirmed that the CAG's views on this issue had been presented to Board.</p> |
| <p>Mr. James agreed with Messrs. Hansen and</p> | <p>Comments noted. The Board has significantly</p> |

| Matters Raised | Task Force/IESBA Response |
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| Waldron, and Ms. de Beer. He noted that IOSCO saw the EQCR issue as an independence-in-appearance issue and that it viewed the EQCR at a similar level of influence as the EP. He noted that it would be disappointing if the Board decided that the EQCR should not have the same five-year cooling-off period as the EP. Mr. Fukushima concurred with Mr. James. | revised its proposals. See accompanying agenda papers. |
| Ms. Robert noted that the EQCR is not regulated in the EU. Accordingly, she had no view on this issue. | Comments considered by the Board. See accompanying agenda papers. |
| Mr. Thompson noted that in the UK, the current provisions are 7+5 for the EQCR and 5+5 for the EP. Nevertheless, he noted that it would be more important to consider the roles of the individuals. | Comments taken into account by the Board in its discussions. |
| Mr. Arteagoitia noted the length of time that the Board had been debating these provisions. He urged the Board to make a decision because it was difficult to justify the continuing debate. He was of the view that a cooling-off period of two or three years was reasonable. He clarified that the EU legislation addresses only the EP, not the EQCR. | Comments noted. |
| Mr. Michel was of the view that a three-year cooling-off period was reasonable. He also urged the Board to make a decision promptly. Ms. Lang agreed with Mr. Arteagoitia that the Board should come to a conclusion on the issue and that further delay would not be advisable. | Comments noted. |
| Ms. Elliott had no comments on this issue. | – |
| Ms. Lopez expressed support for having the same cooling-off period for the EQCR as for the EP to address the perception issue. Mr. Bradbury shared the same view. He noted that he found the Task Force's rationale for having a different treatment for the EQCR unconvincing. He highlighted his own experience in previous audit tenders where the individuals proposed as | Considered by the Board. See above comments and accompanying agenda papers. |

| Matters Raised | Task Force/IESBA Response |
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| EQCR were identified to him. | |
| Ms. Borgerth noted that Brazil has instituted strict provisions to address long association, including mandatory firm rotation. While these provisions are suitable for the Brazilian context, she was not certain that they would work for the IESBA Code. | Comments noted. |
| Ms. Miller noted her perception that the EQCR would have less direct interaction with the client. Accordingly, she was comfortable with a different cooling-off treatment. However, she indicated that she did not feel strongly about any particular position on this issue. | Comments noted. |
| Mr. Muis expressed support for having the same cooling-off treatment for both the EQCR and the EP. He noted that the PIOB had previously expressed regret about the scope of the project in that it did not address the issue of mandatory firm rotation. He acknowledged that coming to a decision on the EQCR issue was more a matter of art than science. However, he noted that the checks and balances were at work in the CAG discussion. | Ms. Orbea noted that this is an area where there is wide divergence of views. Accordingly, she agreed that developing a solution was not a science. |
| APPLICABILITY OF LONGER COOLING-OFF PERIOD TO AUDITS OF LISTED COMPANIES OR ALL PIEs | |
| Ms. McGeachy commented that a large number of PIEs are currently audited by SMPs worldwide. She was of the view that layering the proposals over current regulatory provisions at the jurisdictional level would complicate implementation and have detrimental consequences. For these reasons, she encouraged the Board to limit the proposed provisions to audits of listed entities only. | Comments taken into account. See accompanying agenda papers. |
| Mr. Hansen supported Ms. McGeachy's view and considered that it might be particularly important to the Board's desire for convergence across jurisdictions. He commented that there was so much disparity across jurisdictions that it might be best to concentrate on listed entities. He | See response to Ms. McGeachy above. |

| Matters Raised | Task Force/IESBA Response |
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| expressed the view that it was with listed entities that the public interest is at greatest stake and where the most damage could be caused if an individual were to lose his or her independence. | |
| OTHER COMMENTS | |
| Mr. Greene asked that the Code's long association provisions be clarified in relation to time-on and time-off engagements. In particular, he suggested that an individual's time on the audit should be cumulative and that the time-off period should be calculated consecutively. He also suggested that the provisions should expressly apply to the individual and not to the firm so as to prevent a move of an individual from one firm to another bypassing the provisions. | Ms. Orbea indicated that the word "consecutive" had been added to the relevant paragraph in the draft provisions to address the first situation raised by Mr. Greene. She also explained that an additional clause had been included in the revised proposals to address an individual's length of service as a KAP at a prior firm. |
| Mr. Dalkin noted that in public sector audits, it is quite common that an individual serves on the audit of a particular governmental entity for more than seven years as EP. He wondered whether the proposals addressed this situation. He felt that there would need to be practical considerations regarding partner rotation in public sector audits. | Ms. Orbea indicated that Section 291 applied to public sector audits. |
| Mr. Hansen was of the view that the Task Force should address situations where jurisdictions have more stringent legislation or regulation addressing the topic of long association. On the issue of mandatory firm rotation, he wondered how this could be integrated into the proposals. Finally, he wondered whether there was any research regarding the extent to which SMPs perform audits of PIEs and listed entities. He noted that in the US, there are certain exceptions for firms that have less than a predetermined number of partners. He suggested that reflecting on a similar approach for the Code might assist in achieving a better balance. Ms. McGeachy was of the view that making the split between listed entities and PIEs might be a better and | Comments taken into account in accompanying agenda papers. |

| Matters Raised | Task Force/IESBA Response |
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| fairer approach than drawing a line in terms of a specific number of partners in a firm. | |

Matters for CAG Consideration

7. CAG Representatives are asked for views on the matters for consideration in Agenda Item B-1.

Material Presented – CAG Paper

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| Agenda Item B-1 | Issues paper |
| Agenda Item B-2 | Comparison of the EP and EQCR roles (for reference) |
| Agenda Item B-3 | Long Association Provisions in Section 290 (Mark-Up from ED) |
| Agenda Item B-4 | Long Association Provisions in Section 290 (Clean) |