

Meeting: IESBA CAG
Meeting Location: New York, USA
Meeting Date: March 6, 2017

Agenda Item G-3

Report Back – Long Association

Objective of Agenda Item

1. To report-back on the September 2016 and January 2017 CAG discussions.

Project Status and Timeline

2. The Appendix to this paper provides a history of previous discussions with the CAG on this topic.
3. In August 2014, the IESBA released an Exposure Draft (ED), [*Proposed Changes to the Code of Ethics for Professional Accountants Related to Provisions Addressing the Long Association of Personnel with an Audit or Assurance Client*](#). In December 2015, the IESBA concluded on many aspects of its proposals in both extant Sections 290¹ and 291,² taking into account respondents' comments on the ED and the IESBA's discussions with the CAG and other stakeholders. However, the IESBA determined to issue for re-exposure (re-ED) new or revised proposals concerning three specific matters in relation to extant Section 290 only: (a) the length of the cooling-off period for the engagement quality control reviewer (EQCR) on an audit of a public interest entity (PIE); (b) circumstances where jurisdictions have established different legislative or regulatory requirements addressing long association (the "jurisdictional clause"); and (c) how long to cool off in circumstances where an individual has served in a combination of engagement partner (EP), EQCR and other key audit partner (KAP) roles during the seven-year time-on period.
4. In February 2016, the IESBA issued the re-ED, [*Limited Re-exposure of Proposed Changes to the Code Addressing the Long Association of Personnel with an Audit Client*](#). In September 2016, the IESBA reached agreement on the provisions pertaining to the remaining three matters that were included in the re-ED, taking into account respondents' feedback on the re-ED as well as input from the CAG. Subsequently, in early November 2016, the Public Interest Oversight Board (PIOB) communicated a number of concerns regarding the revised provisions, primarily regarding their perceived complexity and a perceived limited improvement in the cooling-off provisions due to permitted exceptions. As a result of discussions between senior representatives of the IESBA and the PIOB, the PIOB's concerns were narrowed down to three key areas, namely:
 - (a) The jurisdictional clause;
 - (b) The exception that would permit under certain conditions an audit engagement team for a PIE

¹ Extant Part B – Professional Accountants in Public Practice, Section 290, *Independence – Audit and Review Engagements*

² Extant Part B, Section 291, *Independence – Other Assurance Engagements*

to consult with an individual who previously acted as EP or EQCR on the audit engagement and has already served two years of the cooling-off period if they have taken on a primary role as a technical specialist in their firms; and

- (c) The need for transitional provisions relative to the effective date.
5. In December 2016, the IESBA finalized changes to the revised provisions to respond to the PIOB concerns. A January 2017 staff-prepared [Basis for Conclusions](#) explains the significant issues raised by respondents on the proposals in the re-ED, and how the IESBA has addressed them. It also explains the final changes to the revised provisions in response to the PIOB concerns.
 6. The revised provisions will not be formally released until after they have been restructured under the new Structure format. The restructuring exercise will not change the substance of the provisions. As noted in **Agenda Item G-1**, the proposed restructured provisions are included in the January 2017 ED, [Improving the Structure of the Code of Ethics for Professional Accountants—Phase 2](#) (Structure ED-2). Structure ED-2 is open for comment through **May 25, 2017**. **CAG member organizations are strongly encouraged to respond to Structure ED-2.**

September 2016 and January 2017 CAG Discussions

7. Below are extracts from the draft minutes of the September 2016 and January 2017 CAG discussions on the topic,³ and an indication of how the Task Force or IESBA has responded to CAG Representatives' comments.

September 2016

Matters Raised	Task Force/IESBA Response
COOLING-OFF PERIOD FOR THE EQCR ON PIE AUDITS	
Mr. Hansen noted that he had originally supported the bifurcation between listed and non-listed PIEs with a longer cooling-off period for EQCRs in the former case. While he continued to believe this would be appropriate, he understood the concerns raised on the re-ED proposal. Accordingly, he accepted the IESBA's revised position on the matter. He felt that it was time to finalize the provisions. Mr. Waldron agreed with Hansen that it was time to move forward and complete the project.	Support noted.
Expressing a personal view, Mr. Inuma agreed with the revised provision. He acknowledged the difficulty of finding a cooling-off period that would	Point accepted.

³ The draft September 2016 and the January 2017 CAG minutes will be approved at March 2017 IESBA CAG meeting.

Matters Raised	Task Force/IESBA Response
<p>satisfy all stakeholders. He suggested that the IESBA consider a review of the revised provision post-implementation.</p>	<p>Mr. Fleck concurred that most stakeholders would agree on the merit of reviewing the revised long association provisions post-implementation.</p> <p>The IESBA has committed to undertaking a post-implementation review of the revised long association provisions as part of its next strategy and work plan to take account <i>inter alia</i> of relevant legislative and regulatory developments as well as experience of the application of the provisions in practice.</p>
<p>JURISDICTIONAL PROVISION</p>	
<p>Mr. Fortin indicated that he understood the rationale for the revised proposal, noting that it had merit from an European Union (EU) perspective. Regarding the reference to an independent regulatory inspection regime, he wondered about the effectiveness of that regime. He added that this would vary depending on the maturity of the regime. He felt that this was a consideration but nevertheless a difficult issue.</p>	<p>Point noted.</p> <p>Mr. Fleck noted that the reference to an “independent” inspection regime was intended to mean its independence from the audit profession. He added that it is outside the scope of the Code to establish criteria regarding the effectiveness of an audit inspection regime.</p>
<p>Regarding the reference to joint audits, Mr. Hansen noted that there are a number of reasons to justify their existence, for example, to address the industry concentration issue, to help SMPs grow, etc. He was of the view that the issue is how to define a joint audit. He felt that there was a need to explain that concept to prevent abuse or manipulation, such as a larger firm in a joint audit doing most of the substantive work, leaving the smaller firm to play only a marginal role.</p>	<p>Point accepted.</p> <p>Mr. Fleck agreed, noting that there must be substance to a joint audit, i.e., both firms taking substantive part in the audit and sharing responsibility for the audit opinion. He indicated that the Task Force would reflect on wording to convey this principle.</p> <p>In the September 2016 close-off document, the IESBA clarified that it intended a joint audit to be one where more than one firm has been engaged in the audit engagement and the audit report is signed by each of the firms.</p>
<p>Ms. Borgerth noted that Brazil has implemented mandatory firm rotation (MFR) for listed entities. She observed that change is always challenging but that this particular requirement in Brazil has brought a healthy fresh look to the audit.</p>	<p>Point noted.</p>

Matters Raised	Task Force/IESBA Response
<p>Mr. Erik Bradbury noted that from a preparer perspective, a change of audit firms is highly disruptive. He felt that it is important to consider whether there are already adequate safeguards to protect auditor independence. Accordingly, he felt that there is a need for evidence that MFR is helpful. He added that he was not aware of studies of the costs versus benefits of MFR.</p>	<p>Mr. Fleck noted that there has been quite an extensive study done by the UK Competitions Authority regarding the burden of MFR on preparers. The study had concluded that there should instead be mandatory retendering.</p>
<p>SERVICE IN A COMBINATION OF ROLES</p>	
<p>Ms. Ceynowa noted that the Public Company Accounting Oversight Board's independence standards require a two-year cooling-off period before a former EP can move into an EQCR role on the same audit engagement. Mr. Thompson agreed this was an issue to be addressed.</p>	<p>Mr. Gunn responded that this particular issue was subject to coordination between the IESBA and IAASB. Both Boards had agreed that there is a gap in the literature that should be addressed but that doing so would require coordination between them.</p> <p>Mr. Fleck noted that it is important to think also about the issue more broadly, for example, from the perspective of the self-review threat.</p>
<p>Mr. Fortin commented that he found the table illustrating the cooling-off periods for different possible combinations of roles very useful. He suggested that it be included in the Basis for Conclusions or FAQs.</p>	<p>Point accepted.</p> <p>The Appendix to the Basis for Conclusions includes a table titled, "Application of Provisions Regarding Service in a Combination of Roles."</p>
<p>Mr. Hansen raised a question as to whether serving on an engagement as an EQCR for one quarter would count as service for one year.</p>	<p>Mr. Siong responded in the affirmative. He indicated that IESBA Staff had already developed an FAQ addressing this question.</p>

January 2017

Matters Raised	Task Force/IESBA Response
<p>Ms. Lang observed that this situation was unhelpful. She expressed interest in how to prevent a recurrence in future. Ms. Elliott concurred, noting the importance of the lessons learned and for timely PIOB feedback to avoid a repeat of the situation.</p>	<p>Mr. Fleck responded that it would be premature to answer the question of how to avoid a recurrence in future, except to note that both IESBA and PIOB leaderships were committed to taking steps to avoid such recurrence.</p>
<p>Mr. Linuma expressed surprise that the PIOB was about to veto the document and wondered whether this would have been the first time with an IESBA standard.</p>	<p>Dr. Thomadakis responded in the affirmative.</p>
<p>Referring to the sunset clause, Mr. Thompson wondered if the EC will have changed its rules within five years after the revised long association provisions in the Code become effective. He was doubtful it would have done so. Ms. Robert wondered how the proposed review of the revised provisions would be undertaken.</p>	<p>Mr. Fleck responded that it would be inappropriate to attempt to forecast how the EU Audit Regulation would develop over the five years after the revised provisions become effective. However, the IESBA would review how jurisdictions that apply a 7/2 or 7/3 regime, like Australia, are receptive to a 7/5 regime. In addition, the IESBA would need to reflect on how the whole area of long association has evolved in the light of developments around the world concerning mandatory firm rotation, mandatory retendering, etc. On that basis, the IESBA would need to take a view as to whether to revisit the long association provisions in the Code. Any changes to those provisions as a result of this review would be subject to normal due process.</p>
<p>Messrs. Michel and Sobel expressed support for the revised provisions and for moving forward, believing that this was the best outcome achievable in the circumstances.</p>	<p>Support noted.</p>

8. Representatives are asked to note the report backs.

Material Presented – FOR IESBA CAG REFERENCE PURPOSES ONLY

- Close-off Document: [Changes to the Code Addressing the Long Association of Personnel with an Audit or Assurance Client](#)
- Basis for Conclusions: [Changes to the Code Addressing the Long Association of Personnel with an Audit or Assurance Client](#)

- Exposure Draft: [Improving the Structure of the Code of Ethics for Professional Accountants—Phase 2](#)
- Supplement to Structure ED-2, [Restructuring Changes to Long Association Close-off Document](#)

Appendix

Project History

Project: Long Association

Summary

	CAG Meeting	IESBA Meeting
Project commencement	April 2013 September 2013	December 2012 June 2013 September 2013
Development of proposed international pronouncement for Phase I (up to exposure)	October 2013 March 2014 June 2014	December 2013 April 2014 July 2014
Exposure Draft	August 2014 – November 12, 2014	
Consideration of significant comments on Exposure Draft	March 2015 September 2015	January 2015 April 2015 June/July 2015 October 2015 November/December 2015 March 2016 June 2016 September 2016 December 2016
Re-Exposure Draft	February 2016 – May 9, 2016	
Consideration of significant comments on Re-Exposure Draft	September 2016 January 2017 (teleconference)	June 2016 September 2016 December 2016 January 2017 (teleconference)

CAG Discussions: Detailed References

<p>Project Commencement</p>	<p><u>April 2013</u> See IESBA CAG meeting material here and CAG meeting minutes (section G).</p>
<p>Development of Proposed International Pronouncement (Up to Exposure)</p>	<p><u>October 2013</u> See IESBA CAG meeting material and CAG meeting minutes (section B). <u>March 2014</u> See IESBA CAG meeting material and CAG meeting minutes (section D). <u>June 2014</u> See IESBA CAG meeting material and CAG meeting minutes (section B). See report-back on June 2014 discussion.</p>
<p>Consideration of Respondents' Comments and Development of Revised Proposals</p>	<p><u>March 2015</u> See IESBA CAG meeting material and CAG meeting minutes (section E). <u>September 2015</u> See IESBA CAG meeting material and CAG meeting minutes (section B). See report back on September 2015 discussion. <u>September 2016</u> See IESBA CAG meeting material and CAG minutes at Agenda Item A-1 (section E) See report back on September 2016 discussion at paragraph 7. <u>January 2017</u> See IESBA CAG teleconference material and CAG minutes at Agenda Item A-2 See report back on January 2017 discussion at paragraph 7.</p>