

Audit Policy Update

March

HIGHLIGHTS

- Theme of the month: Audit Reform
- European Parliament calls for mandatory 7-year audit rotation
- UK parliament calls for splitting of large audit firms
- The Netherlands reviews its audit market

Theme of this issue: Audit Reform

Below you find an overview of **Accountancy Europe's** work dealing with the changes brought about by the EU rules on statutory audit since these started to apply in June 2016.

Member States' Implementation of New EU audit rules – February 2019

Over 2.5 years after the implementation deadline, we present an updated state of play of this process in 30 European countries, including 28 EU Member States. We have further analysed Member States' decisions and visualised the outcomes for the key options regarding providing non-audit services, mandatory audit firm rotation and public oversight.

[Read more](#)

Organisation of public oversight of the audit profession – February 2019 update

This survey presents the impact of the revised EU statutory audit rules on how the public oversight of statutory auditors and audit firms is organised. It follows up on our 2015 survey.

Designated public oversight bodies have the ultimate responsibility for the oversight of the audit profession. They can delegate certain tasks to other authorities and professional bodies. Our findings show that the national public oversight bodies now carry out many activities previously in the competence of the professional bodies.

[Read more](#)

Auditor reporting of KAMs in European banks

Communicating Key Audit Matters (KAMs) in the auditor's report is a relatively recent requirement to support the quality of audits. It responds to the growing demand for more transparency and insight in the audit process.

Our survey provides insights on auditor's reporting of KAMs for more than 60 European banks. It aims to facilitate communication between banks, auditors and stakeholders on this important new requirement.

[Read more](#)

Definition of Public Interest Entities in Europe – February 2019 update

What is the definition of Public Interest Entities (PIEs) across Europe and what has changed with the new EU statutory audit rules? We provide an overview of the PIE definitions applicable across European countries and the differences amongst them. In addition, we provide insight into the number of PIEs in each country. This publication follows up on our previous survey from 2014.

[Read more](#)

European Union news

MEP asks the European Commission to separate audit firms – 6 March

A Spanish liberal MEP, Ramon Tremosa i Balcells (ALDE/Spain) has [asked](#) the European Commission whether it sees the dominance of the Big Four on the audit markets as a problem.

He specifically asks the Commission what measures it has undertaken to **address “competition problems”**, and whether it would consider a legal separation between auditors of financial statements and non-audit service providers.

In his [reply](#), European Commission's Vice-President **Valdis Dombrovskis** emphasises that the EU's existing audit legislation already includes measures such as prohibition of non-audit services and mandatory audit firm rotation of 10 years. However, given that the new rules only became applicable on 17 June 2016, the impacts of these new provisions are not yet fully effective.

He thus concludes that the Commission will closely monitor the audit market and intends to evaluate the audit legislation's impacts before deciding whether or not to propose additional measures. Any prospective changes to the audit legislation would only take place during the mandate of the next Commission, which starts in November 2019.

European Parliament calls for mandatory 7-year audit rotation – 27 March

The European Parliament set up a so-called TAX3 Committee in March 2018 in the aftermath of Paradise Papers, Panama Papers and other tax leaks and scandals that shed light into tax avoidance and evasion practices. The Committee's objective was to investigate and come up with legally non-binding recommendations to enable Europe to better fight against such practices.

The European Parliament's TAX3 Committee has now adopted its [final report](#) and recommendations for rendering the EU more resilient against tax evasion, tax avoidance and money laundering. The report passed with a margin of 505 votes in favour, 63 votes against and 87 abstentions.

Among the many other tax-specific recommendations, the MEPs also adopted a paragraph calling for mandatory seven-year audit rotation in order to fight against conflicts of interest. This paragraph, which was initially proposed by the Centre-Left S&D Group, passed by a margin of 351 in favour and 296 against. This means that a number of liberal and conservative MEPs voted against their own party lines and aligned with the Left on this issue.

Since the TAX3 report is legally non-binding, the European Commission and the EU Member States do not have to take its recommendations into account. However, the Committee's work does have political weight and influence. The Plenary vote that now took place concludes the TAX3 Committee's work, although the European Parliament intends to set up a permanent tax Committee for the next parliamentary term.

ESMA publishes enforcement report, describes its 2018 audit work – 27 March

The European Securities and Markets Authority (ESMA) has published its [Annual Report](#) on the enforcement and regulatory activities of accounting enforcers within the EU.

On auditing, ESMA outlines its activities in CEAOB in 2018. Although not a voting member of CEAOB, ESMA has contributed to the running of the CEAOB sub-groups and in particular the one chaired by ESMA on equivalence assessments of public oversight systems of third countries. ESMA focused in particular on facilitating international cooperation between EU Member States and third countries in this area.

The sub-group focused on the dialogue with the audit oversight authorities of third-countries for the equivalence and adequacy assessment, and such work is expected to progress further in 2019.

Moreover, ESMA responded in 2018 to the Monitoring Group's consultation on Strengthening the Governance and Oversight of International Audit-related Standard-setting Boards (IAASB) in the Public Interest.

National developments

Netherlands: AFM review of the Dutch audit market – February

The Dutch Authority for the Financial Markets (AFM) has conducted a [study](#) into the vulnerabilities in the structure of the audit sector with the objective to contribute to the debate on the audit quality. The study concludes that especially the demand side of the market, the revenue and the business model of audit firms contain aspects that could have a negative effect on audit quality.

Following this, on 21 November 2018, the Dutch government announced that an independent committee would be set up to carry out work on the future of the audit sector. The objective is to come up with improvement measures and alternative structural models, i.e. the committee will investigate how audit quality could be improved and it should identify potential legislative changes to achieve this as well as their feasibility.

On 1 February 2019, the *Plan of action of the Dutch Committee for the future of the accountancy sector* was made public. The Committee intends to publish their preliminary analyses and findings in the second half of 2019 and final ones at the end of 2019.

Audit regime in the UK to be transformed with new regulator – 11 March

The UK intends to set up a [new audit and accounting regulator](#) to replace the current Financial Reporting Council (FRC). This new regulator will be called Audit, Reporting and Governance Authority (ARGA).

ARGA will have a new mandate, new leadership and stronger powers set down in law, and will for the first time:

- Be a statutory body with powers such as those to direct changes to accounts to be made, rather than applying to court to do so, and more comprehensive, visible reviews for greater transparency
- Have strategic direction and duties to protect the interests of customers and the public by setting high standards of statutory audit, corporate reporting and corporate governance, and by holding companies and professional advisors to account
- Regulate the biggest audit firms directly (rather than those being delegated)

Background

This decision came as a result of the [Independent Review of the FRC](#) led by Sir John Kingman. In parallel, there are three other reviews related to the UK audit market being carried out:

- Competition and Markets Authority's (CMA) review into the statutory audit market
- Brydon Review into UK Audit Standards
- The UK House of Commons' Business, Energy and Industrial Strategy (BEIS) Committee review into the future of audit (more details provided below)

AUDIT FIRMS SCRAP 'CLIENTS' TO WORK WITH 'ENTITIES' – 11 March

FT [writes](#) that KPMG UK has introduced a formal policy that requires staff to refer to the companies it audits as an “audited company” or “audited entity”, instead of “client”. The policy was introduced in November 2018 in an attempt to reinforce the notion that the firm's ultimate clients are the shareholders of the companies it audits, rather than company directors.

Other large audit firms are expected to follow suit, FT reports.

UK Parliament calls for a split of large audit firms – 2 April

The UK House of Commons' Business, Energy and Industrial Strategy (BEIS) Committee has in its [new report](#) called on the Competition and Markets Authority (CMA) to split up the Big Four audit firms.

BEIS conducted an investigation into the UK's recent high-profile accounting and auditing failures such as Carillion, BHS and Patisserie Valerie. The now-published report and recommendations are the outcome of this investigation.

The key recommendations include:

- “Legal separation” of audit staff from the rest of the businesses. After 3 years, if this legal separation fails to produce improvements in culture, independence and transparency, CMA should implement a “full structural break-up” of the B4 into audit and non-audit businesses
- Mandatory seven-year audit rotation. This is the exact same proposal as the European Parliament's TAX3 Committee put forward (see article above)
- Consider introduction of a cooling-off period of 3 years during which non-audit services could not be offered after an audit engagement had ended
- Introduction of a segmented market cap for FTSE 350 market

International

Basel committee calls for external checks on bank loans – 3 March

According to FT, Basel Committee [wants](#) banks' risk weightings to be externally audited in an effort to stop errors and cheating.

Bill Coen, secretary-general of the Basel Committee, said that “involving external audit to play a role in assessing a bank’s risk weightings is a very interesting prospect” and that there is “merit in having another line of defence to ensure assets are [given] the proper risk weighting.”

IAASB

Below are the currently open consultations and exposure drafts of the International Auditing and Assurance Standards Board (IAASB) to which Accountancy Europe plans to respond:

- [Consultation on IAASB Future Strategy and Work Plan](#), deadline to respond is 4 June 2019
- [Consultation on Extended External Reporting \(EER\) Assurance](#), deadline to respond is 21 June 2019
- [ED on International Standard on Quality Management \(ISQM\) 1](#), deadline to respond is 1 July 2019
- [ED on ISQM 2](#), deadline to respond is 1 July 2019
- [ED on International Standard on Auditing \(ISA\) 220: Quality Management for an Audit of Financial Statements](#), deadline to respond is 1 July 2019

Accountancy Europe news

AAPG work programmes, new Chair and Vice-Chairs

As from 2020, Christian Orth from Germany will become the new Chair of Accountancy Europe’s Audit and Assurance Policy Group (AAPG), replacing Myles Thompson from the UK. Another novelty is that starting from 2019, the work of the AAPG will focus on five work programmes. Each of these work programmes will be led by a newly appointed Vice-Chair (see table below). We are thankful for their commitment and wish them a lot of success!

Work programme	Vice-Chair
Audit Reform review	Christian Orth (Vice-Chair for 2019 only) Germany Nicolas Pfeuty France
Assurance and other services	Anne Adrain United Kingdom
Future of audit	David Herbinet United Kingdom
IAASB and PCAOB standards	David Isherwood United Kingdom
SME audit	Kai Morten Hagen Norway