

EISNERAMPER

IRELAND

EU Audit Reform - FAQ's



17 June 2016

1. What is a Public Interest Entity (“PIE”)?

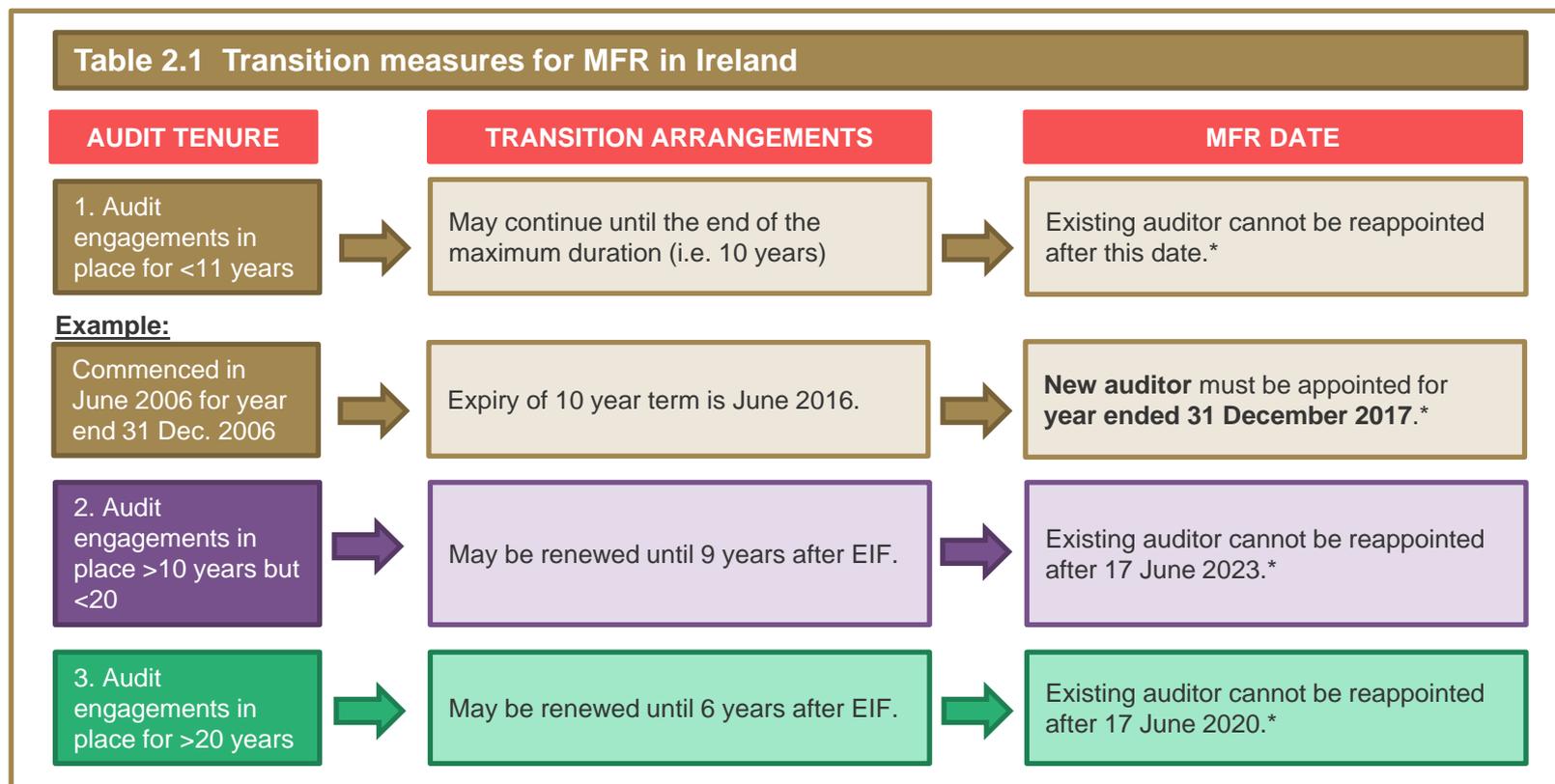
- i. All entities that are both governed by the law of a Member State and listed on a **regulated market** (includes both equity and debt issuers);
 - **Note:** In Ireland there are multiple markets on which issuers (i.e. Companies, Funds and Debt issuers) can have their securities listed on the ISE, e.g. the **Main Securities Market (MSM)** is a **regulated market** as defined under the Markets in Financial Instruments Directive (MIFID) whereas the **Global Exchange Market (GEM)** is an **exchange-regulated market** as defined under MiFID.
 - *Example:* A debt issuing SPV incorporated in Ireland under Irish law and listed on the MSM **is a PIE.**
 - *However:* A debt issuing SPV incorporated in Ireland under Irish law and listed on the GEM **is NOT a PIE.**
- ii. All credit institutions in the EU, irrespective of whether they are listed;
 - **Note:** *A credit institution is an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account.*
 - **Credit Unions are excluded from the EU PIE definition of credit institutions.**
- iii. All insurance undertakings in the EU, irrespective of whether they are listed and irrespective of whether they are life, non-life, insurance or reinsurance undertakings.
- iv. Entities deemed by Member States to be PIEs.



2. How does this impact me as a Director of a PIE?

i. Mandatory Audit Firm Rotation for PIEs

- There is now a mandatory **10-year audit firm rotation** for all PIEs in the EU subject to certain transition arrangements.
- If your Audit Firm has been in place for a period of 10 years or longer you now need to put **transition arrangements** in place to appoint a new audit firm. **Mandatory Firm Rotation** (MFR) is subject to certain transition arrangements and will apply to the audits of financial statements for the financial years commencing on or after 17 June 2016.
- The legislation phases in requirements for MFR depending on the length of the existing audit relationship on the date the legislation enters into force (EIF) (i.e. 17 June 2014). Where the existing audit tenure is 10 years or less, the regulation applies in full. Where the existing audit tenure is between 11 and 20 years on 17 June 2014, the PIE cannot reappoint the incumbent auditor after 17 June 2023. Where the existing audit tenure is equal to 20 years or more on 17 June 2014, the PIE cannot reappoint the incumbent auditor after 17 June 2020. Table 2.1 sets out a summary of the transition measures.



* Where joint audits are performed there is an option to extend the audit tenure.



2. How does this impact me as a Director of a PIE (cont'd)?

ii. **Blacklisted services** – restrictions on the provision of certain non-audit services by PIE auditors

- The statutory auditor of a PIE cannot directly or indirectly “provide any prohibited non-audit services (“NAS”) **to the audit entity, to its parent undertaking or to its controlled undertaking within the EU.**” The NAS restrictions will become applicable from 17 June 2016 onwards.

Prohibited non-audit services

A. Tax services:

- Preparation of tax forms;
- Payroll tax;
- Customs duties;
- Identification of public subsidies and tax incentives unless support from the statutory auditor or audit firm in respect of such services is required by law;
- Support regarding tax inspections by tax authorities unless support from the statutory auditor or audit firm in respect of such inspections is required by law;
- Calculation of direct and indirect tax and deferred tax; and
- Provision of tax advice.

B. Services that involve playing a part in the management or decision making of the audited entity (guidance suggests this includes services such as ‘working capital management, providing financial information, business process optimisation, cash management, transfer pricing, creating supply chain efficiency and similar’).

C. Bookkeeping, preparing accounting records and financial statements.

D. Payroll services.

E. Designing and implementing internal control or risk management procedures related to the preparation and/or control of financial information or designing and implementing financial IT systems.

F. Valuation services, including valuations performed in connection with actuarial services or litigation support services.

G. Legal services, with respect to:

- The provision of general counsel;
- Negotiating on behalf of the audit entity; and
- Acting in an advocacy role in the resolution of litigation.

H. Services related to the audit entity’s internal audit function.

I. Services linked to the financing, capital structure and allocation, and investment strategy of the audited entity, except providing assurance services in relation to the financial statements, such as the issuing of comfort letters in connection with prospectuses issued by the audited entity.

J. Promoting, dealing in or underwriting shares in the audited entity.

K. Human resources services with respect to:

- Management in a position to exert significant influence over the preparation of the accounting records or financial statements that are the subject of the statutory audit, where such services involve: (i) Searching for, or seeking out candidates for such positions, or (ii) Undertaking reference checks of candidates for such positions;
- Structuring the organisation design; and
- Cost control.



2. How does this impact me as a Director of a PIE (cont'd)?

Potentially permitted services

A number of tax services, as well as valuation services, may still be provided in certain cases, subject to a Member State derogation that requires the audit committee to conclude that the services in question comply with the following:

- they have no direct or have immaterial effect, separately or in the aggregate, on the audited financial statements;
- the estimation of the effect on the audited financial statements is comprehensively documented and explained in the additional report to the audit committee referred to in Article 11; and
- the principles of independence laid down in Directive 2006/43/EC are complied with by the statutory auditor or the audit firm.

This derogation is another Member State option and therefore is unlikely to be applied consistently across the EU. However, **tax services relating to payroll tax and customs** duties are not included in the Member State option and therefore **are never permitted**.

Permitted services

All other services are allowed, subject to the approval of the audit committee following an assessment of the threats to independence and the safeguards in place to mitigate or eliminate those threats.

A cap on permissible NAS of 70% of the average of the fees paid in the last three consecutive financial years for the statutory audit(s) of the audited entity and, where applicable, of its parent undertaking, its controlled undertakings and of the consolidated financial statements of that group of undertakings. The cap would only apply in the fourth consecutive year; the clock will be reset if in one year no NAS were provided. During the first three consecutive years, no cap applies.

Permitted services may include:

- Services that will not be covered by audit procedures;
- Strategy consulting;
- Assurance services including the issuing of comfort letters in connection with prospectuses issued by the audited entity; and
- Limited human resources services, excluding those pertaining to management or staff in a position to exert significant influence over the preparation of the accounting records or financial statements that are the subject of the statutory audit.

Permitted services contd.

The Financial Reporting Council in the UK are due to issue an update on a consultation they carried out which proposed a "white list" of non-audit services that could be provided, to the prohibition of all other non-audit services. The proposed activities include:

- Reports required by competent authorities/regulators supervising the audited entity, where the authority / regulator has either specified the auditor to provide the service or identified to the entity that the auditor would be an appropriate choice for service provider;
- Audit and other services provided as auditor of the entity, or as 'reporting accountant', in relation to information of the audited entity for which a reasonable and informed third party would conclude that the understanding of the entity obtained by the auditor for the audit of the financial statements is relevant to the service, and the nature of the service would not compromise the auditor's independence and objectivity. Services could include:
 - audit and other services relating to public reporting as reporting accountant on financial or other information of the audited entity in a prospectus or circular;
 - services, including private reporting, that are customarily performed by the reporting accountant to support statements made by the directors, disclosures in a prospectus or circular or, in the case of premium listed issuers, to support confirmations provided by the entity to a regulatory body;
 - audit and other assurance services relating to public reporting on other information issued by the entity, such as reports on information in the front of annual reports not covered by the auditor's report on the financial statements.



3. Do I need to take any action?

Yes; if you are one of the following stakeholders in a PIE:

- i. Director and/or Audit Committee member.
- ii. Investors, Asset Managers or Originators.
- iii. Audit Firm.

4. What do I need to do?

i. Director and/or Audit Committee member

- a) Decide how the new requirements for regular audit tendering and auditor rotation should be implemented by the PIE.
- b) Put in place a clear and efficient process for when an audit tender is launched, such as opening the process up to firms willing to participate and ensuring that all tenderers can participate on a level playing field.
- c) Reconsider your policies in relation to auditors' independence, including the provision of non-audit services and other areas where the independence of their auditors may be challenged by investors.
- d) Get to know 'challenger firms' better either in the context of future audit tenders and/or to diversify the source of non-audit services.

ii. Investors, Asset Managers or Originators

- a) Develop clear policies in relation to:
 - the mandatory rotation of audit firms;
 - audit tendering including which firms should be considered and key criteria for the selection of auditors;
 - the provision of non-audit services;
 - the independence requirement of Audit Committee members;
 - regular assessments on the performance of auditors.
- b) Engage with PIEs and their Audit Committees to ensure that the new requirements on Audit Committees, notably in relation to their responsibilities and reporting obligations, are implemented in a way that enhances investor confidence.
- c) Organise appropriate communication with PIEs and their Auditors within the context of extended audit reports and enhanced reporting to Audit Committees.
- d) Express support for the fair consideration of non-Big 4 auditors for appointment by PIEs and ensure that all tenderers have participated on a level playing field.
- e) Actively enquire about auditors' selection process to ensure they are fair, transparent and robust, and that firms are demonstrably selected on the basis of merit.



What do I need to do? (cont.)

iii. Audit Firm

- a) Develop procedures with other firms to facilitate the handover of audit files upon rotation. For example could a “Permanent File” be handed over upon rotation? Currently under Irish legislation, it is permitted for the incumbent auditor to allow the incoming auditor access to the audit files.
- b) Increase their investment in audit innovation in relation to audit services, notably in the way audits work and share, and communicate findings with Audit Committees and investors.
- c) If a challenger firm, it should be willing to submit proposals for a significant number of PIE audits each year and to invest time and resources to develop relationships with PIEs.
- d) Ensure effective engagement with Regulators and investors on audit clients and on auditing issues generally.
- e) Commit to working with other firms and other stakeholders with a view to enhancing audit quality across the market.

For further information please see the [European Commission's FAQs](#).



