Setting the scene on the Audit reform and related developments

| 1 June 2016

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EU audit market reform
Introduction

- The EU audit market reform legislation was published in the Official Journal of the European Union on 27 May 2014, in 24 languages (each language version has equal binding force).
- The legislation will be applicable in all EU Member States and in the countries of the European Economic Area (EEA), including Iceland, Liechtenstein and Norway.
- The legislation aims to improve audit quality and restore investor confidence in financial information by reinforcing the independence and objectivity of auditors, improving the communication channels between the auditor, the audit committee and the audited entity and enhancing the role of the audit committee.
- Two forms of legislation:
  - *Directive - Amends the current Statutory Audit Directive, applying to "all' statutory audits – will need to be transposed into national law by each EU Member State*
  - *Regulation - Requirements will govern statutory audits of PIEs. It cross-refers to the Directive, brings additional requirements for the audits of PIEs, and will apply throughout the EU from the effective date*
- Two-year period for implementation into law of each of the Member States is underway

Effective date: as from 17 June 2016.

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Recap of key provisions

Topic	EU legislation
Public interest entities (PIEs)	• EU companies listed on regulated market + governed by EU law • Credit institutions • Insurance undertakings • Member state option to designate additional entities as PIE
Mandatory firm rotation (MFR) and tendering	• 10 years maximum + Member State option to extend to 20 years (with tender) • Transitional periods for statutory audit services started before entry in force of regulation
Non-audit services (NAS)	• Prohibited list approach (similar to IESBA) but with additional restrictions on Tax and Advisory (near ban) • Member State option to add to NAS restrictions • 70% cap on non-audit services, applies to audit firm • Cooling in period (prior FY) for 1 type of service • Member State option to allow certain tax and valuation services • Audit committee approval required for NAS that is not prohibited
Expanded audit opinion	• Now includes description of most significant assessed risk of material misstatement, auditors response to these and key observations • Declaration that no prohibited NAS were provided & that auditor is independent • Interlinked with ISA 701 on key audit matter disclosure (slide 6)
Member State options	• PIE definition • Rotation period and extension • Additional prohibited services • Allow certain tax and valuation services (subject to criteria) • Stricter % cap

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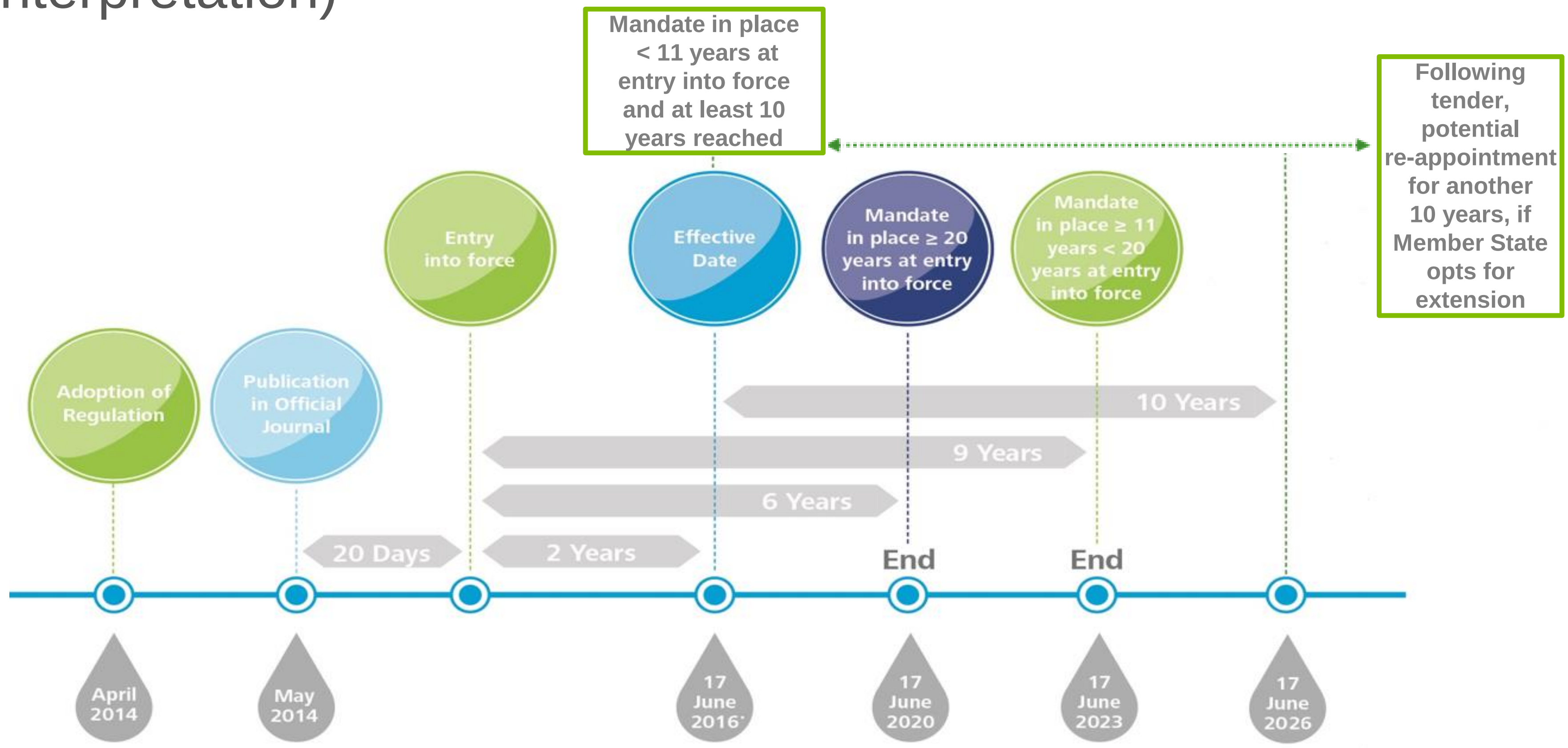
Timeline for transitional measures (EC's current interpretation)



** EC interpretation (2 September 2014 letter): mandates of less than 11 years that have reached 10 year mark (or less if Member State opts to reduce the 10 year period) by the effective date must end by that date, except if Member State opts to extend. Such mandates that have not yet reached 10 year mark by the effective date must end or tender (if permitted) when the 10 year mark is reached.*

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Impact on Audit Committees of PIEs (or Boards if no ACs)

Topic	Impact
Audit Committees	• PIEs are required to have an audit committees but there are exemptions (member state option) for certain PIEs such as UCITS and AIFs • If such PIEs avail to exemption then all responsibilities fall on equivalent committee or full Board
Enhanced responsibilities of audit committees	• Monitor the statutory audit and inform the Board of the outcome • Monitor the financial reporting process • Monitor effectiveness of internal controls and risk management • Auditor selection process and recommendation to the Board • Review and monitor auditor independence including approval of non-audit services
Expanded auditor reporting from auditor to AC	• Report to audit committee

Auditing Standards Developments
Expanded Auditors Report (ISA 701)

Topic	New Standard
New requirement	• Parallel to EU Regulation requirements for audit reports of PIEs, new auditing standard ISA 701 • Communicating **Key Audit Matters** (“KAM”) in the Auditor’s Report – no longer boilerplate audit opinion • KAM is defined as “Those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period.”
Scope	• Audits of **listed** entities
Objective of change	• to provide **greater transparency** to users of financial statements on the auditor’s assessment of what matters were considered as most significant in the audit and how these were addressed
Timing	• **Effective date** will be periods ending on or after 15 December 2016. For Luxembourg, the CSSF may delay the effective date to align with the deadline of the EU audit reform regulation
Impact of Boards/Audit Committees	• Discussions with auditor on key audit matters that will be reported • Will provide users with a basis to further engage Boards/ACs about certain matters relating to the entity, the audited financial statements, or the audit that was performed

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