



Mr Michel Barnier
Commissioner Internal Market and Services
European Commission
200 Rue de la Loi
1049 Bruxelles

14 October 2011

Dear Commissioner,

I would like to share with you some serious concerns which we have on forthcoming proposals in the area of audit policy, following your 12 September intervention at the European Parliament.

BUSINESSEUROPE supports the efforts to ensure that European companies have access to high quality audits and that auditors operate independently. Efforts to further develop the audit market are welcome even though we foresee some practical difficulties. Having said that, we are concerned that a number of complementary measures for the audit market that are being discussed now may have undesirable consequences, such as an increase in the costs of audits and a significant lowering of the overall quality of audits.

This is especially true for measures regarding mandatory rotation of audit firms, mandatory joint audits, limits to – or ban of – the provision of non-audit services and the possible introduction of “Pure Audit Firms”. We have similar concerns about proposals relating to indications on Audit Reports.

We believe that before formally adopting legislative proposals in this area, further dialogue with stakeholders is necessary as high quality audits at reasonable costs are vital for European businesses. We explain these issues in more detail in the appendix to this letter.

We hope that you share our concerns and recommendations and remain at your disposal should you wish to discuss this subject further.

Yours sincerely,

Philippe de Buck



APPENDIX

Mandatory joint audits

Mandatory joint audits do not contribute to audit quality and will cause increased costs for companies – both directly and in terms of internal effort spent to assist two audit firms. As a consequence, when Europe would be the only jurisdiction that mandates joint audits, this would put European industry in a disadvantageous position vis-à-vis its international competitors. Joint audits are currently only used in one Member State in Europe. Quite recently, Denmark abolished mandatory joint audits. The perception from the Danish Government was that joint audits did not contribute to audit quality and did not increase competition in the audit market. Rather, it reduced the number of independent audit firms available.

Non-audit services

Any audit firm, regardless of whether they are joint or sole auditors, has to have the expertise and coverage necessary to audit the entity. The larger the entity the more extensive the requirements. In order to meet these requirements, a great number of specialized skills is required in the organization. In practice, it has been proven that these skills develop and improve when an audit firm also performs non-audit services to non-audit clients. It is equally important that the audit firm has a global coverage that match the audit client. The lack of global reach of smaller audit firms calls into question both practical issues for the conducting of audits but also how they would be able to provide appropriate assurance. A joint audit does not offer a solution, as each audit firm holds joint and severable liability for the entire audit, and thus should have the expertise and coverage to audit all activities if necessary. It would only increase costs for companies and in the end for the shareholders.

Mandatory rotation

Mandatory rotation of audit firms effectively reduces the number of independent audit firms that are available and qualified to bid for an audit. Moreover, the rotation of firms would not improve audit quality since it will lead to a significant loss of knowledge of the audit. Large international groups are so complex that the audit firm needs time to understand all the related intricacies. Moreover, when an audit firm knows that they will have to rotate, the incentive to perform a high quality audit is reduced and it could lead firms to reduce their investment in audit files. Thus neither audit quality nor increased competition in the market is served by a mandatory rotation.

Audit regulators

Audit regulators have a key role to play in increasing audit quality and ensuring independence. Audit regulators were formally introduced with the 8th Directive. This Directive should have been implemented in June 2008 in all Member States and therefore audit regulators are just beginning to mature. When the Directive was introduced, many audit regulators focused on checklists and therefore auditors focused more on procedures than on professional skepticism. We have seen lately that a number of audit regulators increasingly focus on the quality of the audit. Further



measures aimed at audit regulators who increasingly focus on the quality of the audit that result in a shift in behavior by the auditors are supported.

International Audit Standards (ISAs)

Generally,, BUSINESSEUROPE finds it very important that audit regulation is based on international accepted principles. BUSINESSEUROPE welcomes suggestions to formally introduce ISAs directly within the European auditing framework, binding auditors how they conduct their audit. The introduction should not change the fact that management responsibilities are still governed only by company law. This was already envisaged with the 8th Directive. Also, it is key that changes in the Audit Opinion / Audit Report on the financial statements are in conformity with international regulations and principles and that audit reports should be governed by the same framework at global level in order to increase global transparency. Audit reports should be short and to the point. It should be clear whether they are qualified or not, and the audit report should not address issues that rightfully should be addressed by accounting or other reporting standards. We recommend that account is taken of developments with the International Auditing and Assurance Standards Board (IAASB) on these issues.

Conclusion

BUSINESSEUROPE considers that most measures under consideration do not reflect the real issues. In our view, the Commission has still to demonstrate the role of auditors in the development of the crisis. Concerns have been raised but these have not been substantiated by factual information showing a breakdown in controls or unsuitable regulatory framework. Such proof is necessary for proposing any corrective measures. Criticism on the functioning of auditors relates primarily to the shortcomings and the complexity of the IFRS reporting framework. Auditors cannot solve these problems and should not be required to do so. Therefore, BUSINESSEUROPE believes that most proposals that are currently under consideration will on balance not solve the perceived problems with the functioning of auditors. Proper measures must be accompanied by initiatives that allow the application of professional judgment, instead of the current practice of an IFRS compliance review.
