



Fédération des Experts
Comptables Européens

Press Release

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EUROPE'S ACCOUNTANTS ASK COMMISSION, COUNCIL OF MINISTERS & PARLIAMENT TO ADDRESS WEAKNESSES IN PROPOSED EU AUDIT DIRECTIVE

FEE publishes profession's proposals for improvements in oversight, audit standards, independence & liability

Brussels, 31 March 2004: In its formal response to the European Commission's proposal to revise the Eighth EU Directive on Auditing, the representative organisation of the European accountancy profession, FEE, today published a comprehensive submission to the Commission, the Council of Economic and Finance Ministers and the European Parliament.

In it, FEE strongly supports the initiative to modernise the law on auditing, but voices concerns to the Commission, the Council of Ministers and Parliament that some provisions designed to improve oversight, audit standards, independence and liability are too weak. The FEE submission makes concrete proposals to strengthen the proposed audit reforms.

FEE – Fédération des Experts Comptables Européens (FEE) - has 41 member bodies of professional accountants from 29 countries, representing more than 500,000 accountants in Europe.

Launching FEE's submission on the Revised 8th Directive, the organisation's President, David Devlin said: "auditing is central to ensuring the credibility and reliability of financial reporting. FEE's proposals aim at restoring trust in financial reporting for capital markets. We support many of the proposals in the revised Directive. We note that many of its provisions are consistency with the FEE policy on key issues such as audit committees, international standards on auditing, internal rotation of audit partners and statutory backing for robust quality assurance and inspection."

FEE has, however, identified 4 areas where it believes the Commission's proposals are currently weak and can be improved upon. The European accountancy profession is asking the Commission, Council of Ministers and European Parliament to address its concerns and proposals in the course of formally considering the Revised Directive:

- **FEE Calls For Co-ordinated Oversight:**

"FEE has long been calling for the creation of a European-level body to co-ordinate oversight arrangements at member state level. Unfortunately, the proposed Directive lacks clarity regarding the organisation of the European co-ordination. It is imperative that this co-ordination body be visibly structured in the public interest and involve all stakeholders appropriately.

Furthermore, for public interest entities, the Commission wishes to exclude the audit profession from national oversight systems. FEE believes that a separate oversight for listed companies will introduce a false dichotomy, without any evidence that this could improve oversight results or enhance the credibility of the mechanism."

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"There is a strong case for the involvement of professionals in the governance of oversight for auditors and audit firms of both listed and unlisted companies. This is confirmed by recent legislation in several EU member states, for example France and Ireland, as well as in Canada."

- **FEE Supports Global Endorsement of Standards:**

"FEE supports global standards in auditing and ethics. We welcome the proposal to apply International Standards of Auditing in Europe. These standards are set under new public interest oversight arrangements that have been enthusiastically endorsed by the Financial Stability Forum. Such endorsement confirms that the public interest will always be upheld in setting these standards.

The requirements of these principle-based standards are already applied in many EU Member States. They are appropriate to the delivery of high quality audits. However, FEE is concerned that the endorsement procedure in the proposed Directive could introduce an unnecessarily costly new procedure. We also consider that the proposal to have a definition of the audit report in the law is inappropriate as such issues should continue to be dealt with effectively in auditing standards."

- **FEE's View on Scope of Services and Rotation of Firms:**

"FEE welcomes the proposal of the Commission to promote the 'threats and safeguard' approach which identifies risks to independence and provides principles as well as detailed prohibitions, rules and guidance to protect auditors' independence.

However, we must also express significant concern over the specific proposals for listed companies, in the areas of *scope of services* and *rotation of audit firms*.

The explanatory memorandum of the Commission's proposals raise the possibility of a general prohibition on provision of non-audit services to audit clients. FEE does not believe that such restrictive rules will improve the quality of audits, which requires a sound understanding of the audited enterprise and the markets in which it operates. Audit related and other appropriate services can provide auditors with additional insight which contributes to the quality of the audit. We once again call on the Commission to clarify the real situation by immediately bringing forward their plans for a study of non-audit services.

The proposed Directive, if adopted, would establish a special regime for public interest entities, including the possible option for member states to require audit firms to rotate every seven years. A few countries in the world, such as Italy, already apply mandatory rotation of firms. The arguments for and against mandatory audit firm rotation concern whether the independence of an audit firm is adversely affected by a firm's long-term relationship with the client and the desire to retain the client. Concerns about the potential effects of mandatory audit firm rotation include whether its intended benefits would outweigh the costs and the loss of company specific knowledge gained by an audit firm through years of experience auditing the client."

"It is widely believed that the costs of mandatory audit firm rotation are likely to exceed the benefits and that the current requirements for audit partner rotation, auditor independence, and other reforms will achieve the intended benefits of mandatory audit firm rotation. Given that there is widespread doubt about the actual effects of such a regime on audit quality, in light of evidence from empirical studies that the risk of audit failure is higher in the first years of an audit, FEE

does not support the specific proposal in the directive on rotation of audit firms. FEE supports a robust system of quality assurance and inspection.”

- **FEE Calls For EU Study on Liability:**

“The risk of catastrophic losses arising from huge claims in relation to audit is a most serious threat to the viability of the auditing profession.

We contend that reform is a major issue in the public interest. It is essential that audit liability fairly and reasonably relates to the consequences of unsatisfactory audit performance. In order to perform high quality audits, the audit profession needs to attract and train individuals of the highest personal qualities, able to address the many complexities of financial reporting and auditing. Such new entrants need to be able to understand properly the businesses which they are auditing and possess the personal qualities of integrity and character necessary to report with candour. Such individuals need to see in auditing the potential for an attractive career with opportunities for undertaking a variety of work and in a framework of reasonably balanced personal risk. FEE therefore urges the European Commission to accelerate its study of this issue,” stated the FEE President.

- Ends -

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Notes for Editors:

1. The European Commission’s proposal for a revised Eight Directive is posted at: http://europa.eu.int/comm/internal_market/en/company/audit/official/index.htm
2. FEE’s comment letters of August, October & December are available to download from: <http://www.fee.be/secretariat/Positionpaper.htm>
3. The **Fédération des Experts Comptables Européens** (FEE) is the representative organisation for the accountancy profession in Europe. It groups together 41 professional bodies from 29 countries. FEE member bodies are present in all fifteen member-states of the European Union, nine European Union candidate countries and three member countries of EFTA. Between them, these bodies have a combined membership of 500.000 individuals, of whom approximately 94% are from EU countries.