

Quality Assurance for Statutory Audit

Background:

In April 1998, FEE published a paper, “Continuous Quality Assurance – Statutory Audit in Europe”, followed by two ‘Round Tables’ in 1998 and 2003 providing a forum to share experiences and ideas on quality assurance in European Union (EU) Member States. The paper set out the results of a study by FEE of the mechanisms for quality assurance of statutory audit in twenty European countries, including all EU Member States. It reflected the considerable work done by professional bodies throughout Europe to develop systems to ensure quality in statutory audit.

In November 2000, the European Commission issued its “Recommendation on Quality Assurance for the Statutory Audit in the European Union: Minimum Requirements” (the EC Recommendation on Quality Assurance), in whose development the 1998 FEE paper was believed to have been instrumental.

In relation to internal quality control, in 2004, the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC) issued International Standard on Quality Control 1 (ISQC1) “Quality control for firms that perform audits and reviews of historical financial information, and other assurance and related services engagements”. This standard required audit firms to establish a system of quality control designed to provide it with reasonable assurance that the audit firm and its personnel comply with professional standards and regulatory and legal requirements, and that auditor’s report issued are appropriate in the circumstances. The FEE survey of 2006 also aimed to review compliance with the core principles of ISQC1.

In December 2006, FEE issued a paper, “Quality Assurance Arrangements Across Europe” based on a survey of quality assurance systems and public oversight arrangements of 29 European countries, as of 1 July 2006.

The study concluded that a significant number of EU Member States were still considering the impact of the Statutory Audit Directive in relation to the creation of a system of public oversight and the implementation of Article 29 on quality assurance. FEE strongly supported public oversight bodies at EU Member State level which, while having the ultimate responsibility, allow for significant delegation to the profession. It was also considered important to have all stakeholders represented in a public oversight body and each of its members should be competent and knowledgeable in the areas relevant to auditing.

FEE found that all countries surveyed except one had a system of external quality assurance in place that covered all audit firms or all statutory auditors. Two different types of quality assurance systems generally operate in Europe. In ‘monitoring reviews’, quality assurance reviews are undertaken by staff employed by a review organisation. In ‘monitored peer review’, the review organisation organises and supervises the reviews to be undertaken by experienced and authorised practitioners of audit firms or statutory auditors. Despite these differences, both systems of monitoring and monitored peer review were considered to comply with the Statutory Audit Directive.

With this study, the profession demonstrated that it is fully committed to achieving consistent high quality in statutory audits in the public interest by well-functioning and effective systems of quality assurance.

(continued overleaf)

Current Status:

On 9 June 2006, the Directive of the European Parliament and of the Council of 17 May 2006 on “Statutory Audit of Annual Accounts and Consolidated Accounts” (the Statutory Audit Directive) was published in the Official Journal of the European Union. It introduces a requirement for all statutory auditors and audit firms to be subject to a system of quality assurance, organised independently from the reviewed statutory auditors and audit firms and subject to public oversight. The requirements of this Directive necessitate changes to the quality assurance arrangements in a number of European countries. The FEE survey of 2006 also focused on these anticipated changes. Although European Union Member States had two years, that was up to mid-2008 to implement the provisions of the Statutory Audit Directive, a considerable number of them still has to do so as at October 2008.

On 6 May 2008, the European Commission issued the “Recommendation on external quality assurance for statutory auditors and audit firms auditing public interest entities”. The Recommendation provided guidance for implementing independent external quality assurance systems for statutory auditors and audit firms conducting an audit of public interest entities, in accordance with Articles 29 and 43 and as defined in Articles 2.13 and 39 of the Statutory Audit Directive.

More details related to the Recommendation are included in the Appendix.

Next Steps:

European Union Member States are requested to inform the European Commission about actions taken in light of this most recent Recommendation by 6 May 2009.

In the light of new international developments, in particular the involvement of appropriate bodies and experts in the execution of inspections, the European Commission intends to evaluate the situation in 2011.

FEE will support the European Commission’s review of the implementation of the Recommendation.

Following the two successful high level conferences on audit regulation of 2006 and 2007 at which external quality assurance was discussed, FEE will organise its third high level conference on audit regulation on 9 December 2008 at which home country oversight, mutual reliance and joint inspections will be discussed.

FEE is also monitoring the work of the IAASB as far as the finalisation of ‘ISA 220 on Quality Control for an Audit of Financial Statements’ and ‘ISQC 1 on Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements’ under the IAASB clarity project is concerned. On 19 September 2008, the IAASB approved these redrafted standards for issue, subject to confirmation by the Public Interest Oversight Board (PIOB) that due process has been followed.

FEE Contact:

Hilde Blomme
 Director of Practice Regulation
hilde.blomme@fee.be

FEE Secretariat:

Fédération des Experts Comptables Européens
 Avenue d’Auderghem 22-28, B-1040 Bruxelles
 Tel: +32 2 285 40 85 - Fax: +32 2 231 11 12 - Web: www.fee.be

About FEE:

FEE (Fédération des Experts Comptables Européens – Federation of European Accountants) represents 43 professional institutes of accountants and auditors from 32 European countries, including all 27 EU Member States.

Appendix:

The European Commission issued the “Recommendation on external quality assurance for statutory auditors and audit firms auditing public interest entities” which provides guidance for implementing independent external quality assurance systems for statutory auditors and audit firms conducting an audit of public interest entities, in accordance with Articles 29 and 43 and as defined in Articles 2.13 and 39 of the Statutory Audit Directive.

No detailed guidance with regard to the external quality assurance systems for statutory auditors and audit firms auditing entities other than public interest entities is provided, for which Article 29 of the Statutory Audit Directive is considered sufficient.

The Recommendation defines certain important terms in more detail:

- An inspector is a reviewer employed by a public oversight authority or another appropriate body to which execution of inspections has been delegated:
 - ⇒ He is subject to independence policies and procedures;
 - ⇒ He has to declare any conflicts of interest;
 - ⇒ He cannot be or be associated with a practising statutory auditor;
 - ⇒ He is subject to a cooling-off period of two years before inspecting auditors or audit firms he was previously associated with;
 - ⇒ He should not be directly remunerated by the reviewed auditor, audit firms or network.
- Professional associations are not directly referred to, except in Recital (7) where they are named together with other appropriate bodies;
- Inspections are quality assurance reviews led by an inspector which are not investigations. They are performed at least every three years based on Article 43 of the Statutory Audit Directive;
- An expert is a natural person, who has specific expertise in financial markets, financial reporting, auditing or other fields relevant for inspections, including practising statutory auditors. He can assist inspectors under the direct control of an inspector. The independence, cooling-off and remuneration provisions of inspectors also apply to experts.

A public oversight authority independent from the profession assumes ultimate responsibility for the external quality assurance system whereby inspections are:

- Either executed by the public oversight authority; or
- Executed by the public oversight authority together with another appropriate body; or
- Delegated to another appropriate body with accountability to the public oversight authority for at least inspection methodologies, inspection reports and assignment of inspectors; or
- On-site reviews are performed by experts who are fully accountable to the public oversight authority, alternated with an on-site review by inspectors at least every six years.

Funding for quality assurance systems should be independent from the profession, be sufficient and mandatory.

Inspections should cover:

- An assessment of the design and effectiveness of the internal quality control systems of the audit firm by;
 - ⇒ Testing of the auditor's or audit firm's compliance with:
 - * Internal quality control policies, procedures and standards;
 - * Applicable auditing, ethical and independence standards;
 - * Relevant laws, regulations and provisions;
 - * Continuing education requirements, including a review of the quantity and quality of resources;
 - * Requirements related to audit fees.
 - ⇒ Review of audit files of public interest entities, primarily selected using a risk-based approach.
- An assessment of the auditor's transparency report.

The public oversight authority is responsible for communicating the outcome of inspections as follows:

- Inspection findings, conclusions and recommendations are properly communicated to and discussed with the inspected auditor or audit firm before issuance of the final inspection report;
- The inspected auditor or audit firm has up to 12 months to follow-up on the recommendation on his internal quality control system;
- In case of inappropriate follow-up, the public oversight authority discloses major deficiencies in internal quality control systems;
- Timely and appropriate public disclosure of any final disciplinary actions taken or penalties imposed, identifying the auditor or audit firm and describing the major deficiencies concerned;
- Timely amendment of significantly misleading transparency reports;
- Annual report including the overall results of the quality assurance system including recommendations, their follow-up, disciplinary actions taken, penalties imposed and other quantitative information.

FEE References:

Continuous Quality Assurance – Statutory Audit in Europe (1998)

http://www.fee.be/search/default_view.asp?content_ref=893

Quality Assurance Arrangements Across Europe (2006)

http://www.fee.be/publications/default.asp?library_ref=4&content_ref=629

European and International References:

Statutory Audit of Annual Accounts and Consolidated Accounts

Directive of the European parliament and of the Council 2006/43/EC of 17 May 2006

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:157:0087:0107:EN:PDF>

External quality assurance for statutory auditors and audit firms auditing public interest entities

European Commission Recommendation 2008/362/EC of 6 May 2008

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:120:0020:0024:EN:PDF>

Proposed ISA 220 (Redrafted), Quality Control for an Audit of Financial Statements ISQC 1 (Redrafted), Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements, September 2008

<http://www.ifac.org/IAASB/Meeting-BGPapers.php?MID=0143&ViewCat=0980>