



CHARTERED ACCOUNTANTS  
AUSTRALIA + NEW ZEALAND

9 May 2016

The Chairman  
International Ethics Standards Board for Accountants  
529 5th Avenue  
6th Floor  
New York 10017  
United States of America

*Submission via IESBA website*

Dear Mr Thomadakis

### **Submission on Exposure Draft: Limited Re-exposure of Proposed Changes to the Code Addressing the Long Association of Personnel with an Audit Client (“the ED”)**

We commend the IESBA’s efforts to promote and enhance objectivity and professional scepticism. We agree it is essential that audit and assurance teams and firms are independent, both of mind and in appearance, of their clients and we support a common international framework for making that assessment. However, as stated in our response to the previous ED on this subject, while we support review of the framework and continuing work to enhance the framework if required due to changing circumstances, we do not support the specific proposals in this ED.

We believe that there has still not been any evidence presented that indicates that increasing the cooling off periods for Engagement Partners (EPs) or Engagement Quality Control Reviewers (EQCRs) will improve audit quality. In contrast we have heard repeated concerns from practitioners and preparers that increasing the cooling off period will increase costs, increase complexity of administration of the rotation process, and potentially drive smaller audit firms out of the market. We do not believe that implementing requirements that will potentially contract the audit market and lead to these consequences can have a positive impact on audit quality.

#### **Inadvertent impacts on the audit market in some jurisdictions**

Our members have repeatedly expressed their views that in Australia and New Zealand, the extension of cooling off periods to five years for EPs and EQCRs will negatively impact audit quality for the following reasons:

- Below the larger firms, introducing a five year cooling-off period may result in a de facto mandatory audit firm rotation if there are an insufficient number of audit partners to manage partner rotation successfully. Given that other proposals in relation to mandatory rotation have largely been aimed at ensuring that the audit market does not become an oligopoly, this proposal appears to be counterintuitive with the objective of having a competitive market.

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- One country that is held up as an example that five year partner rotation is manageable is the US. In the US partner rotation applies only to SEC issuers and has not been extended to PIEs. US SEC issuers, due to the size of the market, are substantially larger than the majority of issuers in our capital markets. Therefore comparisons in relation to the manageability and impacts of the rotation process are not appropriate. In the US audit firms are registered to be able to audit issuers rather than individual partners. We note that in the US, even in relation to US issuers, there are exemptions to rotation requirements for smaller firms (less than 10 audit partners) with small numbers of clients who are registrants (less than five), so the regulator has acknowledged the potential for these requirements to adversely impact the smaller end of the market. We also understand that in Canada the independence code includes an exemption to certain independence requirements for listed entities (including partner rotation) below a certain market capitalization as it was felt requiring those entities to comply with the full requirements of the code would adversely impact those entities and smaller audit firms.
- Even in firms which have sufficient numbers of audit partners to manage rotation, it is likely that increasing the cooling-off period will result in an increase in the number of engagements where the engagement partner is located in a different geographical location to the client and the engagement team. A high level of direct audit partner involvement with the client and the engagement team has been acknowledged to be a key driver of audit quality. Similarly, ECQR need to be able to interact with the engagement team and engagement partner as appropriate. Where partners are geographically separated it becomes more difficult for partners to sustain this level of involvement, and therefore audit quality may be adversely affected.
- In Australia and New Zealand, we are already concerned about a shortage of registered auditors in regional areas. If smaller firms cannot manage rotation, it is likely that they will leave the market. Contraction of the audit market will not enhance audit quality. Firms may have even smaller pools of partners with the appropriate seniority and experience to act as EQCRs which only increases the potential impact of these issues.
- Clients may decide that moving to a firm where they only have to change audit partners rather than change firms altogether is preferable. This could result in partners having to spend additional time in business development activities and securing additional clients. This is time that then cannot be spent on audit quality activities. Clients would also incur additional costs from the time and resources required to conduct a tender process, and then again when a new auditor is selected.

These outcomes could negatively impact audit quality, reducing the progress that the profession has worked hard for over the last decade, which is not in the public interest. Given that there is no evidence that a longer cooling-off period will improve independence, we believe the costs of this proposal clearly outweigh any potential benefits.

### **Practical difficulties**

The coordination of EP and EQCR rotation is already time consuming and costly for firms. Increasing the administrative complexity by introducing an excessive cooling-off period will only increase these costs, even when the audit firm does not change, without increasing audit quality. While our members do not support the increase in cooling off periods for EPs and EQCRs they expressed a view that for practical implementation purposes, a system where the cooling off period is the same for EPs and EQCRs and for listed entities and PIEs is simpler to manage which would minimise the increased costs of changes.

### **Other approaches**

We reiterate our belief, as expressed in our submission on the previous ED, that other approaches which strengthen auditor independence without negatively impacting audit quality, such as a comply or explain model, should be further explored. We do not believe there is an issue in the Australian or New Zealand market with the current requirements in place. The current requirements combined with audit firms' own systems of quality control already achieve the objective of maintaining a robust independence framework. In addition, independent internal and external quality reviews, use of an auditor's expert for specialist areas, natural turnover of audit team and client personnel, provide adequate safeguards.

Should the proposals proceed, our members emphasised the importance of an adequate lead time to enable them to plan for implementation of partner rotation. We also believe that if the proposals are implemented, the board should consider whether other safeguards currently implemented in the code which are largely procedural and appearance driven such as bans on partners holding mortgages with banks they audit, can be removed.

### **About Chartered Accountants Australia and New Zealand**

Chartered Accountants Australia and New Zealand is a professional body comprised of over 115,000 diverse, talented and financially astute members who utilize their skills every day to make a difference for businesses the world over.

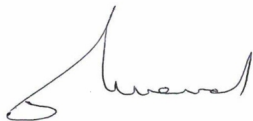
Members are known for their professional integrity, principled judgment, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations.

We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international capital markets.

We are a member of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

The appendix (attached) provides responses to the specific questions raised in the ED. If you have any questions regarding this submission, please contact Liz Stamford (Audit and Insolvency Leader) via email; [Liz.Stamford@charteredaccountantsanz.com](mailto:Liz.Stamford@charteredaccountantsanz.com).

Yours sincerely

A handwritten signature in black ink, appearing to read 'Rob Ward', written in a cursive style.

**Rob Ward AM FCA**  
**Head of Leadership and Advocacy**

## **Appendix: Responses to specific questions**

**Q1. Do respondents agree that the IESBA’s proposal in paragraphs 290.150A and 290.150B regarding the cooling-off period for the audits of PIEs (i.e., five years with respect to listed entities and three years with respect to PIEs other than listed entities) reflects an appropriate balance in the public interest between:**

- (a) Addressing the need for a robust safeguard to ensure a “fresh look” given the important role of the EQCR on the audit engagement and the EQCR’s familiarity with the audit issues; and**
- (b) Having regard to the practical consequences of implementation given the large number of entities defined as PIEs around the world and the generally more limited availability of individuals able to serve in an EQCR role?**

**If not, what alternative proposal might better address the need for this balance?**

We accept that a cooling-off period for the engagement partner and engagement quality control reviewer provides a mechanism for a ‘fresh pair of eyes’ to be introduced to the engagement and to help maintain independence. However, as stated in our response to the previous ED, and given the lack of empirical evidence, the number of years that is appropriate for a cooling-off period is arbitrary. Assurance practitioners have confidence that the current mechanism already provides sufficient safeguards to address the threat to independence of mind from long association. The independence of the EQCR is already protected by the nature of their role, in which they have limited contact with the client and the day to day management and conduct of the audit. We see no need for the cooling off period for EQCRs to be extended.

In our consultations with the director and preparer community, they similarly did not feel there was any issue with the current two year cooling-off period for either EPs or EQCRs. Therefore, we do not support this proposal.

**Q2. Do respondents support the proposal to allow for a reduction in the cooling-off period for EPs and EQCRs on audits of PIEs to three years under the conditions specified in paragraph 290.150D?**

We do not support extending the requirements to PIEs. However, if the requirements are extended to PIEs, then we believe a shorter cooling off period as determined by the local regulators, standard setters and legislators is appropriate.

**Q3. If so, do respondents agree with the conditions specified in subparagraphs 290.150D(a) and (b)? If not, why not, and what other conditions, if any should be specified?**

We believe that the local regulators, standard setters and legislators should be able to develop requirements that they believe are appropriate to support audit quality in their jurisdictions. Therefore we believe that specific requirements to reduce the cooling off period should not be imposed by the code.

**Q4. Do respondents agree with the proposed principle “for either (a) four more years or (b) at least two out of the last three years” to be used in determining whether the longer cooling-off period, applies when a partner has served in a combination of roles, including that of EP or EQCR, during the seven-year time-on period (paragraphs 290.150A and 290.150B).**

We agree that that the principle appears reasonable.