



EU audit reform

On 17 June 2016, new EU statutory audit legislation came into effect. The new audit legislation requires Public Interest Entities (“PIEs”) to rotate their statutory auditor and prohibits the statutory from providing certain non- audit services.

Mandatory firm rotation (“MFR”)

The MFR general requirement is that the initial engagement period for a statutory auditor should not exceed 10 years. Member states can opt to extend this period by a maximum of further 10 years if a tender is undertaken or 14 years if a joint audit is adopted. At the request of the audited entity, the national regulators/supervising authorities can extend the term once for a further two years, in “exceptional circumstances”.

The legislation applies to any PIE; including subsidiaries of multinationals headquarter outside of the EU that falls within the definition of a PIE (see below). The legislation will be applicable in the 28 EU member states as well as Iceland, Liechtenstein and Norway.

Transitional arrangements

The legislation provide for transitional periods depending on the length of the relationship of an entity with its auditor at the date of entry into force of the regulation (i.e. 16 June 2014). Audit engagements are separated into three categories:

- A) If a PIE has the same auditor for 20 years or more (i.e. prior to 16 June 1994) the engagement cannot be renewed with the incumbent auditor on or after **17 June 2020**.
- B) If a PIE has the same auditor for 11 and up to 20 years on 16 June 2014 (i.e., first year that was audited began between 17 June 1994 and 16 June 2003) it may not enter or renew the audit engagement with the incumbent auditor as of **17 June 2023**.
- C) If a PIE has the same auditor for fewer than 11 years, on 16 June 2014 (i.e. after 17 June 2003), engagements will remain applicable until the end of the maximum period. This means that if the auditor was appointed for the financial years starting:
 - Between 16 June 2003 to 17 June 2006: the PIE should retender or rotate by 17 June 2016.
 - After 17 June 2006: the PIE should change or retender when the maximum tenure is reached from the first year of engagement.

The rotation requirements for this tranche of engagements would begin to apply to the first financial year starting on or after 17 June 2016, except if a member state has specifically opted to allow extension to 20 years in case of tendering or 24 years in case of joint audit.



Understanding if your company is an EU PIE or if you have an EU PIE in your group

The PIE concept is not new as an EU PIE definition was already included in the Statutory Audit Directive of 2006. The underlying EU PIE definition has not changed in the new legislation, although its scope has been expanded. The new (2014) PIE definition includes:

1. Companies with transferable securities listed on EU regulated markets (as opposed to all markets in the EU) and governed by the law of an EU member state (requirement is consistent with the same category under Statutory Audit Directive (2006));
2. Credit institutions authorized by EU member states' authorities (requirement is broadly the same as in Statutory Audit Directive (2006) except member states are no longer allowed to exempt non-listed PIEs from the requirements of this category);
3. Insurance undertakings authorized by EU member states' authorities (requirement is broadly the same as in Statutory Audit Directive (2006), except member states are no longer allowed to exempt non-listed PIEs from the requirements of this category);
4. Other entities a member state may choose to designate as a PIE (requirement is consistent with the same category under Statutory Audit Directive (2006))

Therefore, determining if you are an EU PIE is a two-step process:

1. Determine if you are covered by the baseline EU PIE definition.
2. Understand how the Member State of which the law you are governed by has implemented the existing EU PIE definition.

Prohibition of certain non-audit services ("NAS")

The new EY legislation prohibits the statutory auditor of a PIE to provide the PIE, its parent company and any EU controlled entities with a wide range of specific non-audit services.

- a) Tax services, including but not limited to preparation of calculations of direct/indirect taxes and deferred tax. Member states can allow some tax services through local legislation
- b) Services involving the auditor with management or decision-making for the audited entity such as working Capital management, transfer pricing, business process optimization.
- c) Services linked to the financing, capital structure and allocation, and investment strategy of the audited entity
- d) Promoting, dealing in, or under-writing shares in the audited entity
- e) Various Legal Services
- f) Book-keeping and preparing accounting records and financial statements



- g) Payroll services
- h) Designing and implementing internal controls and risk management procedures or financial information
- i) Valuation services. Member states can allow such services under specific conditions.
- j) Internal audit related services

- k) Human resources services regarding structuring of the organization, cost control and recruitment of management personnel which will be involved in the statutory audit,

All other non-audit services are allowed subject to the approval of the PIE's audit committee and to a cap of fees for such services compared to the statutory audit fees.

This publication contains only summary information for general guidance purposes. It is not intended to replace professional advice and judgement, and thus this publication does not constitute advice. The legislation is complex and several areas of the legislation's interpretation may evolve over time. Affected parties may wish to seek legal advice before taking measures to comply with the recently enforced EU legislation.

Contact Persons

Andreas Pittakas
Director, Audit & Assurance Services
a.pittakas@bakertillyklitou.com

George Nicolaides
Director, Business Service Division
g.nicolaides@bakertillyklitou.com

Neofytos Neofytou
Head of Tax Services
n.neofytou@bakertillyklitou.com

Address

Nicosia
Corner C. Hatzopoulou &
30 Griva Digheni Ave.
1060, Nicosia, Cyprus
T: +357 22458500
F: +357 22751648
info@bakertillyklitou.com