



## EUROPEAN COMMISSION - PRESS RELEASE

### **Restoring confidence in financial statements: the European Commission aims at a higher quality, dynamic and open audit market**

Brussels, 30 November 2011 - The 2008 financial crisis highlighted considerable shortcomings in the European audit system. Audits of some large financial institutions just before, during and since the crisis resulted in 'clean' audit reports despite the serious intrinsic weaknesses in the financial health of the institutions concerned. Recent inspection reports by national supervisors have also criticised the quality of audits.

Under the proposals adopted today by the European Commission, this situation is to change by clarifying the role of the auditors and introducing more stringent rules for the audit sector aimed in particular at strengthening the independence of auditors as well as greater diversity into the current highly-concentrated audit market. Furthermore, the Commission is also proposing to create a Single Market for statutory audit services allowing auditors to exercise their profession freely and easily across Europe, once licensed in one Member State. There are also proposals for a strengthened and more coordinated approach to the supervision of auditors in the EU. Taken together, all the measures should enhance the quality of statutory audits in the EU and restore confidence in audited financial statements, in particular those of banks, insurers and large listed companies.

Internal Market and Services Commissioner Michel Barnier said: *"Investor confidence in audit has been shaken by the crisis and I believe changes in this sector are necessary: we need to restore confidence in the financial statements of companies. Today's proposals address the current weaknesses in the EU audit market, by eliminating conflicts of interest, ensuring independence and robust supervision and by facilitating more diversity in what is an overly concentrated market, especially at the top-end."*

## **Background:**

Auditors are entrusted by law to give an opinion on the truth and fairness of the financial statements of the companies they audit. The financial crisis highlighted weaknesses in the statutory audit especially with regards to banks and financial institutions. Concerns around conflicts of interest have been expressed as well as the potential for an accumulation of systemic risk as the market is effectively dominated by four companies ("the Big Four"), namely Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers.

## **Key elements of the proposal:**

The proposals regarding the statutory audit of public-interest entities, such as banks, insurance companies and listed companies, envisage measures to enhance auditor independence and to make the statutory audit market more dynamic. The key measures in this respect are:

**Mandatory rotation of audit firms:** Audit firms will be required to rotate after a maximum engagement period of 6 years (with some exceptions). A cooling off period of 4 years is applicable before the audit firm can be engaged again by the same client. The period before which rotation is obligatory can be extended to 9 years if joint audits are performed, i.e. if the entity being audited appoints more than one audit firm to carry out its audit, thus potentially improving the quality of the audit performed by applying the "four-eyes principle". Joint audits are not made obligatory but are thus encouraged.

**Mandatory tendering:** Public-interest entities will be obliged to have an open and transparent tender procedure when selecting a new auditor. The audit committee (of the audited entity) should be closely involved in the selection procedure.

**Non-audit services:** Audit firms will be prohibited from providing non-audit services to their audit clients. In addition, large audit firms will be obliged to separate audit activities from non-audit activities in order to avoid all risks of conflict of interest.

**European supervision of the audit sector:** In addition, given the global context of audit, it is important that coordination of and cooperation on the oversight of audit networks is ensured both at EU level as well as internationally. Therefore, the Commission proposes that the coordination of the auditor supervision activities is ensured within the framework of the European Markets and Securities Authority (ESMA).

**Enabling auditors to exercise their profession across Europe:** The Commission proposes the creation of a Single Market for statutory audits by introducing a European passport for the audit profession. To this end, the Commission proposals will allow audit firms to provide services across the EU and to require all statutory auditors and audit firms to comply with international auditing standards when carrying out statutory audits.

**Cutting red tape for smaller auditors:** The proposal also allows for a proportionate application of the standards in the case of small and medium-sized companies.

[MEMO/11/856](#)

The proposals can be found at:

[http://ec.europa.eu/internal\\_market/auditing/reform/index\\_en.htm](http://ec.europa.eu/internal_market/auditing/reform/index_en.htm)

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