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Sent electronically to

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EACB Concerns on mandatory rotation of audit firms for financial institutions after six years

Dear Mr. Karim,

The European Association of Co-operative Banks (EACB) understands the intention of European Legislators to improve the quality of audit by providing a robust framework for auditor independence and corporate governance.

In some Member States audit systems of decentralized sectors are characterised by the principle of permanent statutory mandate of associations[1]. Their member audits have proven sound and should thus be acknowledged.

But even where such systems do not exist, we have reservations against the mandatory rotation of audit firms. In particular, we have strong doubts regarding mandatory rotation after 6 years already (9 years in the case of joint audit). We think that this would be counterproductive and will reduce the overall quality of audit.

- Article 33 (2) of the proposed Regulation forces a public interest entity to rotate its statutory auditor after 6 years or 9 years in the case of joint audit. This proposal ignores that newly appointed auditors require a considerable amount of time to familiarise themselves with their new client, particularly clients with a high degree of complexity such as banks. Such measure would reduce the resources of the audit firms and those of the clients. Changing auditors on such short intervals would increase the risk of lower quality of audits with less incentives to focus on longer-term issues.

- We understand that possible approach discussed by some member states in the Council is to limit mandatory rotation after 6 years to financial institutions. First, we do not understand why banks should be subjected to requirements while all other institutions would be excluded. Banks are highly complex businesses that require time for auditors to become familiar with the difficult judgmental areas such as the level of illiquid instruments, the level of impairment provisions, etc… Auditors need to have good knowledge and understanding of the constantly evolving environment in which they operate.

- Mandatory rotation would have negative impacts on smaller banks by increasing the costs, lower the quality of the audit for a couple of years, and thus, endanger the quality of the annual accounts. We do not see that small banks could sustain

[1] According to German and Austrian law of co-operative auditing

such measures as they are already facing many controls and supervisions. In smaller territories, the number of auditors who really understand for instance banking and insurance business, is limited and concentrated only in some audit-companies. The mandatory rotation of the audit company would in that situation be impossible in practise, or would mean that the resources would change from one audit company to another (which in turn, would not increase the independency). In that cases changing the responsible partner within the audit firm as currently required would be sufficient to insure both, the independence of the auditor and a high quality of the audit at the same time.

- The arguments in favour of the mandatory rotation (doubts around the credibility and reliability of the audited financial statements of banks, reinforcing the independence of auditors) do not take into consideration the mandate of auditors. To make judgements on the business model or individual transactions of clients is not the task of the auditors but merely the responsibility of the management of the audited company. The responsibility of the auditor is only to examine the accurate presentation of the transactions made by the audited entity and to make a statement on whether or not the staff and equipment available is sufficient in order to carry out such transactions. We therefore do not share the view that the financial crisis would have been avoided if mandatory rotation of audit firms would have been in place as the auditor cannot stop a client from acquiring for example subprime financial instruments.

- In order to avoid an increase of the burden for small banks, we think that mandatory rotation rules after 6 years (and 9 years in the case of joint audit) for the audit industry should not be implemented.

Should you have any questions, we would be happy to clarify the issues more precisely.

Yours sincerely,

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<u>Copy to:</u>

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