

Regulatory News Alert

EU Audit Market Reform – Go!

Law of 23 July on the Audit Profession

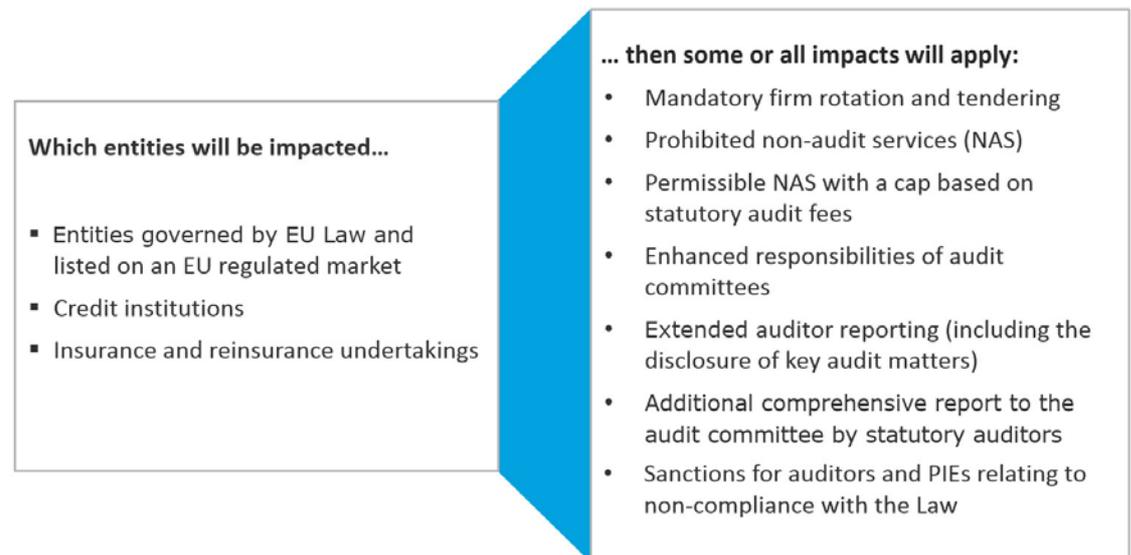
28 July 2016

On 22 March 2016, the *Chambre des Députés* published draft Law 6969 (“the draft Law”) implementing:

- **Directive 2014/56/EU** amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts (“the Directive”); and
- **Regulation (EU) No 537/2014** on specific requirements regarding statutory audit of public-interest entities (“the Regulation”).

The Luxembourg Law implementing the Audit Market Reform was **published on *Mémorial A* on 28 July 2016**. The new requirements will impact Public Interest Entities (PIEs), their parent undertakings and controlled undertakings within the European Union.

EU Audit Market Reform in a nutshell



Overview of new requirements

<p>Mandatory firm rotation and tendering</p>	<p>Luxembourg draft Law foresees a maximum duration of audit engagement of 20 years, with mandatory tendering after 10 years. PIEs are to perform a transparent audit tendering process with a close involvement of the audit committee when a tender does occur. A cooling-off period of 4 years shall be respected after the end of the statutory audit services before audit firm can undertake the audit of the entity again.</p> <p>The final Law did not retain the proposal for the minimum duration of audit firm appointments for statutory audits as a three-year term. Therefore, there is no minimum duration for audit firm appointment.</p>
<p>Prohibited non-audit services (NAS)</p>	<p>The EU regulatory package on Audit Market Reform introduces a “black list” approach regarding non-audit services provided by the audit firm and its network. This provision is enforceable for accounting periods beginning after 17 June 2016. The Luxembourg Law exercises the option to authorize certain tax and valuation services by the entity’s audit firm, subject to certain conditions.</p>
<p>Permissible NAS with a cap based on statutory audit fees</p>	<p>Fees for permissible NAS provided by the audit firm to the audited entity, its parent undertaking or its controlled undertakings (EU), where performed for three consecutive financial years, must not exceed, each year, 70% of the average annual fees charged by that audit firm in the last three consecutive financial years for statutory audits of the PIE, its parent or controlled undertakings (EU+world), and of the group consolidated financial statements.</p> <p>The audit committee shall approve non-audit services that are not prohibited. These provisions are enforceable for periods beginning after 17 June 2019.</p>

<p>Enhanced responsibilities of audit committees</p>	<p>Each PIE shall establish an audit committee composed of non-executive members of administrative body and/or members of the supervisory body and/or members appointed by the general meeting of shareholders.</p> <p>The following entities could be exempted to set up an audit committee:</p> <ul style="list-style-type: none"> - Small or medium-sized undertakings and PIEs with reduced market capitalisation (functions of the audit committee are performed by an administrative or supervisory body); - PIEs with a body performing equivalent functions; - PIEs which is a subsidiary if the requirements are fulfilled at group level; - PIEs which are Undertakings for Collective Investment in Transferable Securities (UCITS) or Alternative Investment Funds (AIFs); - PIEs the sole business of which is to act as an issuer of asset backed securities; - Banks whose shares are not admitted to trading on a EU regulated market, and which have, in a continuous or repeated manner, issued only debt securities admitted to trading in a regulated market, provided that the total nominal amount of all such debt securities remains below EUR 100 000 000 and that it has not published a prospectus; <p>The audit committee is responsible for the procedure for the selection of the auditor / audit firm, and it shall perform the pre-approval of permissible services.</p>
<p>Extended auditors reporting & additional report to audit committee</p>	<p>In respect of the Regulation and the International Standard on Auditing (ISA) 701 Communicating Key Audit Matters in the independent auditor's report, the extended audit report applicable to PIEs shall provide a description of the most significant assessed risks of material misstatement, including assessed risks of material misstatement due to fraud, a summary of auditor's response to those risks, and key observations arising with respect to those risks.</p> <p>Auditors of PIEs will have to prepare a more comprehensive report directly to the audit committee, applicable for accounting periods starting as of 17 June 2016 year end, including:</p> <ul style="list-style-type: none"> - More detailed information on the results of the audit; - Disclosure of quantitative level of materiality applied to perform the statutory audit, materiality level(s) for particular classes of transactions, account balances or disclosures, and qualitative factors used to determine materiality; and - Report and explain judgments about events or conditions identified during the audit that may cast significant doubt on the entity's ability to continue as a going concern and whether they constitute a material uncertainty, and provide a summary of all measures that have been taken into account when making a going concern assessment.

Sanctions	Sanctions are foreseen for auditors and members of management bodies and audit committees of PIEs in case of non-compliance with the Law (up-to EUR 1 million or 5% of annual turnover)
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