Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC (Text with EEA relevance)

REGULATION (EU) No 537/2014 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

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(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Economic and Social Committee[(1)],

Acting in accordance with the ordinary legislative procedure[(2)],

Whereas:

(1) Statutory auditors and audit firms are entrusted by law to conduct statutory audits of public-interest entities with a view to enhancing the degree of confidence of the public in the annual and consolidated financial statements of such entities. The public-interest function of statutory audit means that a broad community of people and institutions rely on the quality of a statutory auditor's or an audit firm's work. Good audit quality contributes to the orderly functioning of markets by enhancing the integrity and efficiency of financial statements. Thus, statutory auditors fulfil a particularly important societal role.

(2) Union legislation requires that the financial statements, comprising annual financial statements or consolidated financial statements, of credit institutions, insurance undertakings, issuers of securities admitted to trading on a regulated market, payment institutions, undertakings for collective investment in transferable securities (UCITS), electronic money institutions and alternative investment funds be audited by one or more persons entitled to carry out such audits in accordance with Union law, namely: Article 1(1) of Council Directive 86/635/EEC[(3)], Article 1(1) of Council Directive 91/674/EEC[(4)], Article 4(4) of Directive 2004/109/EC of the European Parliament and of the Council[(5)], Article 15(2) of Directive 2007/64/EC of the European Parliament and of the Council[(6)], Article 73 of Directive 2009/65/EC of the European Parliament and of the Council[(7)], Article 3(1) of Directive 2009/110/EC of the European Parliament and of the Council[(8)], and Article 22(3) of Directive 2011/61/EU of the European Parliament

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and of the Council[9]. Moreover, point (1) of Article 4(1) of Directive 2004/39/EC of the European Parliament and of the Council[10] also requires that the annual financial statements of investment firms be audited when Directive 2013/34/EU of the European Parliament and of the Council[11] is not applicable.

(3) The conditions for the approval of the persons responsible for carrying out the statutory audit as well as the minimum requirements for carrying out such statutory audit are laid down in Directive 2006/43/EC of the European Parliament and of the Council[12].

(4) On 13 October 2010 the Commission published a Green Paper entitled 'Audit Policy: Lessons from the Crisis', which launched a wide public consultation, in the general context of financial market regulatory reform, on the role and scope of audit and how the audit function could be enhanced in order to contribute to increased financial stability. That public consultation showed that the rules of Directive 2006/43/EC regarding the carrying out of the statutory audit of annual and consolidated financial statements of public-interest entities could be improved. The European Parliament issued an own-initiative report on the Green Paper on 13 September 2011. The European Economic and Social Committee also adopted a report on that Green Paper on 16 June 2011.

(5) It is important to lay down detailed rules with a view to ensuring that the statutory audits of public-interest entities are of adequate quality and are carried out by statutory auditors and audit firms subject to stringent requirements. A common regulatory approach should enhance the integrity, independence, objectivity, responsibility, transparency and reliability of statutory auditors and audit firms carrying out statutory audits of public-interest entities, contributing to the quality of statutory audits in the Union, thus to the smooth functioning of the internal market, while achieving a high level of consumer and investor protection. The development of a separate act for public-interest entities should also ensure consistent harmonisation and uniform application of the rules and thus contribute to a more effective functioning of the internal market. These strict requirements should be applicable to statutory auditors and audit firms only insofar as they carry out statutory audits of public-interest entities.

(6) The statutory audit of cooperatives and savings banks is characterised in some Member States by a system that does not allow them to choose their statutory auditor or audit firm freely. The audit association to which the cooperative or savings bank belongs as a member is obliged by law to carry out the statutory audit. Such audit associations act on a non-profit-making basis without pursuing commercial interests, as results from their legal nature. In addition, the organisational units of these associations are not associated with a common economic interest, which could jeopardise their independence. Accordingly, Member States should have the possibility to exempt cooperatives within the meaning of point (14) of Article 2 of Directive 2006/43/EC, savings banks or similar entities as referred to in Article 45 of Directive 86/635/EEC or their subsidiaries or legal successors from this Regulation provided that the principles of independence laid down in Directive 2006/43/EC are complied with.

(7) The level of fees received from one audited entity and the structure of fees can threaten the independence of a statutory auditor or an audit firm. Thus, it is important to ensure that audit fees are not based on any form of contingency and that, when the audit

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fees from a single client including its subsidiaries are significant, a specific procedure involving the audit committee is established to secure the quality of the audit. If the statutory auditor or the audit firm becomes excessively dependent on a single client, the audit committee should decide on the basis of proper grounds whether the statutory auditor or the audit firm may continue to carry out the statutory audit. When taking such decision, the audit committee should take into consideration, inter alia, the threats to independence and the consequences of such decision.

(8) The provision of certain services other than statutory audit (non-audit services) to audited entities by statutory auditors, audit firms or members of their networks may compromise their independence. Therefore, it is appropriate to prohibit the provision of certain non-audit services such as specific tax, consultancy and advisory services to the audited entity, to its parent undertaking and to its controlled undertakings within the Union. The services that involve playing any part in the management or decision-making of the audited entity might include working capital management, providing financial information, business process optimisation, cash management, transfer pricing, creating supply chain efficiency and the like. Services linked to the financing, capital structure and allocation, and investment strategy of the audited entity should be prohibited except the provision of services such as due diligence services, issuing comfort letters in connection with prospectuses issued by the audited entity and other assurance services.

(9) It should be possible for Member States to decide to allow the statutory auditors and the audit firms to provide certain tax and valuation services when such services are immaterial or have no direct effect, separately or in the aggregate, on the audited financial statements. Where such services involve aggressive tax planning, they should not be considered as immaterial. Accordingly, a statutory auditor or an audit firm should not provide such services to the audited entity. A statutory auditor or an audit firm should be able to provide non-audit services which are not prohibited under this Regulation, if the provision of those services has been approved in advance by the audit committee and if the statutory auditor or the audit firm has satisfied itself that provision of those services does not pose a threat to the independence of the statutory auditor or the audit firm that cannot be reduced to an acceptable level by the application of safeguards.

(10) With a view to avoiding conflicts of interest it is important that the statutory auditor or the audit firm, before accepting or continuing an engagement for a statutory audit of a public-interest entity, assess whether the independence requirements are met, and in particular whether any threats to independence arise as a result of the relationship with that entity. The statutory auditor or the audit firm should confirm its independence annually to the audit committee of the audited entity and should discuss with that committee any threat to its independence as well as the safeguards applied to mitigate those threats.

(11) Directive 95/46/EC of the European Parliament and of the Council[(13)] should govern the processing of personal data carried out in the Member States in the context of this Regulation and such processing of personal data should be subject to the supervision

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of the Member States' competent authorities, in particular the public independent authorities designated by the Member States. Any exchange or transmission of information by competent authorities should comply with the rules on the transfer of personal data as laid down in Directive 95/46/EC.

(12) A sound engagement quality control review of the work carried out in each statutory audit engagement should be conducive to high audit quality. Therefore, the statutory auditor or the audit firm should not issue his, her or its audit report until such an engagement quality control review has been completed.

(13) The results of the statutory audit of a public-interest entity should be presented to the stakeholders in the audit report. In order to increase the confidence of stakeholders in the financial statements of the audited entity, it is particularly important that the audit report be well-founded and solidly substantiated. In addition to the information required to be provided under Article 28 of Directive 2006/43/EC, the audit report should in particular include sufficient information on the independence of the statutory auditor or the audit firm and on whether the statutory audit was considered capable of detecting irregularities, including fraud.

(14) The value of statutory audit for the audited entity would be particularly enhanced if the communication between the statutory auditor or the audit firm, on the one hand, and the audit committee, on the other hand, were reinforced. Further to the regular dialogue during the carrying out of the statutory audit, it is important that the statutory auditor or the audit firm submit to the audit committee an additional and more detailed report on the results of the statutory audit. This additional report should be submitted to the audit committee no later than the audit report. Upon request, the statutory auditor or the audit firm should discuss key matters which have been mentioned in the additional report with the audit committee. In addition, it should be possible to make such additional detailed report available to competent authorities responsible for the oversight of statutory auditors and audit firms upon their request, and to third parties where national law so provides.

(15) Statutory auditors or audit firms already provide competent authorities supervising public-interest entities with information on facts or decisions which could constitute a breach of the rules governing the activities of the audited entity or an impairment of the continuous functioning of the audited entity. However, supervisory tasks would be facilitated if supervisors of credit institutions and insurance undertakings and their statutory auditors and audit firms were required to establish an effective dialogue with each other.

(16) Regulation (EU) No 1092/2010 of the European Parliament and of the Council[14] established the European Systemic Risk Board (ESRB). The role of the ESRB is to monitor the build-up of systemic risk in the Union. Given the information that statutory auditors and audit firms of systemically important financial institutions have access to, their experience could help the ESRB in its work. Therefore an annual forum for dialogue between statutory auditors and audit firms, on the one hand, and ESRB, on the other, on a sectoral, anonymised basis should be facilitated by this Regulation.

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(17) In order to increase the confidence in, and the liability of, the statutory auditors and the audit firms carrying out the statutory audit of public-interest entities, it is important that the transparency reporting by statutory auditors and audit firms be increased. Therefore, statutory auditors and audit firms should be required to disclose financial information, showing in particular their total turnover divided into audit fees paid by public-interest entities, audit fees paid by other entities and fees for other services. They should also disclose financial information at the level of the network to which they belong. Statutory auditors and audit firms should provide additional supplementary information on audit fees to competent authorities with a view to facilitating their supervisory tasks.

(18) It is important that the role of the audit committee in the selection of a new statutory auditor or audit firm be reinforced, in the interest of a more informed decision of the general meeting of shareholders or members of the audited entity. Hence, when making a proposal to the general meeting, the administrative or supervisory body should explain whether it follows the preference of the audit committee and, if not, why. The recommendation of the audit committee should include at least two possible choices for the audit engagement and a duly justified preference for one of them, so that a real choice can be made. In order to provide a fair and proper justification in its recommendation, the audit committee should use the results of a mandatory selection procedure organised by the audited entity, under the responsibility of the audit committee. In such selection procedure, the audited entity should not restrict statutory auditors or audit firms with a low market share from presenting proposals for the audit engagement. Tender documents should contain transparent and non-discriminatory selection criteria to be used for the evaluation of proposals. Considering, however, that this selection procedure could entail disproportionate costs for undertakings with reduced market capitalisation or small and medium-sized public-interest entities having regard to their size, it is appropriate to relieve such undertakings and entities from the obligation of organising a procedure for the selection of a new statutory auditor or audit firm.

(19) The right of the general meeting of shareholders or members of the audited entity to choose the statutory auditor or the audit firm would be of no value if the audited entity were to enter into a contract with a third party providing for a restriction of such choice. Therefore, any clause of a contract entered into by the audited entity with a third party regarding the appointment or restricting the choice to particular statutory auditors or audit firms should be considered null and void.

(20) The appointment of more than one statutory auditor or audit firm by public-interest entities would reinforce the professional scepticism and help to increase audit quality. Also, this measure, combined with the presence of smaller audit firms in the audit market would facilitate the development of the capacity of such firms, thus broadening the choice of statutory auditors and audit firms for public-interest entities. Therefore, the latter should be encouraged and incentivised to appoint more than one statutory auditor or audit firm to carry out the statutory audit.

(21) In order to address the familiarity threat and therefore reinforce the independence of statutory auditors and audit firms, it is important to establish a maximum duration of the