

## MANDATORY ROTATION OF AUDIT FIRMS ENDANGERS AUDIT QUALITY

**The FEE Study: “Mandatory Rotation of Audit Firms”** reviews the most significant reports by governments, regulatory bodies and academics on this subject. The survey includes reports from Italy, Spain, the UK, the US and Australia. It sets out the main arguments made in these reports in favour of such rotation as well as against.

- The overwhelming majority of studies found that the mandatory (i.e. forced) rotation of audit firms inadvertently threatens audit quality.
- The superficially attractive idea of mandatory rotation could in fact undermine the EU’s work to build public trust in financial reporting. By allowing mandatory rotation as an add-on to the effective auditor independence measures already proposed in the revision of the Eighth Company Law Directive, audit quality could be undermined:
  - an increased threat to audit quality in the first years of audit, due to reduced knowledge of client operations (for the ‘new’ auditor); and
  - an unscrupulous management who are deliberately misleading their auditors will find that regular change of auditor will reduce the chances of their schemes being discovered.
- While cost should not be a decisive argument when set against audit quality, mandatory rotation would lead to:
  - increased financial costs for business; and
  - an increase in time management must allocate to meeting with the ‘new’ auditors getting to know the business.
- Interestingly, artificially enforced rotation of audit firms has been shown to increase market concentration in the large firms.
- The US considers that mandatory external rotation is not an appropriate solution. Italy is the sole EU member state actively applying mandatory rotation of audit firms.
- FEE supports effective reform that strengthens auditor independence - reforms that contribute to audit quality and which are in the public interest. Therefore FEE supports the package of proposals in the EU’s draft 8th Directive which will enhance the role of the audit committee in relation to the appointment and oversight of the company-auditor relationship and introduce requirements for quality control, audit partner rotation and independent public oversight of the profession. These reforms will provide effective safeguards, strengthening auditor independence in Europe.
- Hence, FEE does not support supplementing the auditor independence reforms currently proposed in the EU with an additional requirement for mandatory rotation of audit firms. It would bring very little incremental benefit for audit independence or increased competition but risks creating real threats to audit quality.

### About FEE

*The Fédération des Experts Comptables Européens is the representative organisation for the accountancy profession in Europe. FEE’s membership consists of 41 professional institutes of accountants from 29 countries. FEE member bodies represent more than 500,000 accountants in Europe.*

### Contact:

Hilde Blomme  
 Director of Practice  
 Regulation  
 Rue de la Loi 83  
 B-1040 Bruxelles  
 Belgium

tel: +32 2 285 40 85

fax: +32 2 231 11 12

email:

[hilde\\_bloomme@fee.be](mailto:hilde_bloomme@fee.be)