

European Group of Auditors' Oversight Bodies
(EGAOB)

Guidance Paper

on the Cooperation Between Competent Authorities within the EU

2009

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1. INTRODUCTION

This guidance paper of the European Group of Auditors' Oversight Bodies (EAOB) sets out a common approach for cooperation between the competent authorities of Member States with respect to audit firm and auditor oversight within the European Union, as required by the Directive 2006/43/EC¹ (the Statutory Audit Directive). This paper will be reviewed annually.

2. DESIGNATION OF A SINGLE CONTACT POINT

Article 33 of the Directive states that *Member States shall ensure that regulatory arrangements for public oversight systems permit effective cooperation at Community level in respect of Member States' oversight activities*. To that end, each Member State shall make one entity specifically responsible for ensuring that cooperation.

Therefore the most effective solution would be that each Member State designates a single competent authority as a single contact point for the transfer of any information between competent authorities. This authority should be the public oversight body (=EAOB member) to enable a smooth functioning of the exchange of information. This would also prevent any perception of a potential issue of conflict of interest (see Article 35(2) of the Directive).

In some Member States the system of public oversight comprises several competent authorities, having their own “ultimate responsibility” for specific areas of audit oversight. In such a case the first contact should be established with the entity in the Member State that is the EAOB member that has been designated as single contact point. That entity would then transfer the request, as necessary, to the relevant competent authority. Further contacts following the request could then take place directly with the competent authority having the specific responsibilities.

It should not be necessary in all cases for requests for information to be between members of the management board of competent authorities. To facilitate effective communication between Member States under Article 36, a competent authority in a Member State should be able to accept a request for information made by someone in another competent authority that has been given an appropriate delegated authority by the management board of their organisation.

The EAOB agreed to draw up a contact list of persons with delegated authority to act on behalf of the competent authority that is designated as the single contact point in the Member State for exchange purposes.

3. LANGUAGE

Competent authorities in Member States should communicate if possible in English, other than where an alternative language is mutually convenient. Accompanying

¹ Directive 2006/43/EC on statutory audit of annual accounts and consolidated accounts and amending Council Directives 78/660/EEC and 83/349/EEC: http://ec.europa.eu/internal_market/auditing/directives/index_en.htm

information that is not in English can be transferred in the original language, although the transferring competent authority at its own discretion can decide to provide the receiving competent authority with a brief overall summary of that information in English.

4. TYPES OF ‘INFORMATION’

According to Article 36(1) of the Directive, “*competent authorities shall exchange information*”. Information covered by professional secrecy may not be disclosed to any other person or authority except by virtue of the laws, regulations or administrative procedures of a Member State (Article 36(2) of the Directive). However, this article shall not prevent competent authorities from exchanging confidential information (Article 36(3) of the Directive).

Thus, according to the Directive, any (confidential) information can in principle be exchanged between competent authorities. The table below contains a non-exhaustive list of the kind or nature of information that can in principle be exchanged according to the requested purposes (for inspections, investigations, etc.).

| Purpose of transfer | Kind/nature of information |
|--------------------------------|---|
| Registration / Approval | Personal data Information relevant for registration and (possible) deregistration of audit firms and/or auditors, e.g. registration decisions regarding statutory auditor(s) / audit firm(s) |
| Inspection / Quality assurance | Information about (pending) inspections, e.g. inspection reports Audit working papers |
| Discipline | Information about (pending) disciplinary proceedings against the statutory auditor(s) / audit firms(s), e.g., results of the disciplinary proceeding |
| Investigation | Information about (pending) investigations Results of investigative proceedings against the statutory auditor(s) / audit firm(s) Information about (pending) administrative law |

5. FREE TRANSFER OF CONFIDENTIAL INFORMATION

Member States may not add conditions relating to the exchange of information between competent authorities additional to those set out in Article 36 of the Directive. To do otherwise would hinder effective cooperation between Member States and defeat the objective of minimum harmonisation across the EU. In particular:

- (1) No specific bilateral arrangement, such as a memorandum of understanding, needs to be concluded between competent authorities of different Member States in order for information, including confidential information, to be transferred from one competent authority to another.
- (2) The competent authority transferring the information must rely on confidentiality rules of the competent authority receiving the information, provided that the information is used by the receiving competent authority for the exercise of functions within the scope of the Directive and/or in the context of administrative or judicial proceedings specifically related to the exercise of those functions (Articles 36(2), 36(3) and 36(4) of the Directive). This means that consent by the transferring competent authority is not necessary where the information is transferred to “*another person or authority*”... “*by virtue of the laws, regulations or administrative procedures of [the receiving] Member State*”.
- (3) Where information is to be transferred by the receiving competent authority at its discretion to another authority in that Member State, e.g. the securities regulator, for other purposes, the receiving competent authority should seek in advance the explicit consent of the transferring competent authority for the transfer of information to that other authority. The competent authority that transferred the information initially should be given the right to express consent or rejection to the further transfer.
- (4) If there are legal requirements in place which require the receiving competent authority to pass on the information to another authority, then an objection to the transfer would be of no avail. Nevertheless in such a case the receiving authority should use its best efforts to protect the confidentiality of non-public information received from the transferring competent authority. The receiving competent authority should wherever possible alert the transferring authority prior to complying with the legal requirement and provide a brief notification when it has been done.
- (4) Intra EU transfers do not need approval by the domestic data protection authorities. Article 1 of the Data Protection Directive (Directive 95/46/EC) states that Member States shall neither restrict nor prohibit the free flow of personal data between Member States.

6. COOPERATION BETWEEN COMPETENT AUTHORITIES

6.1. General

According to Article 36(1) of the Directive competent authorities shall cooperate with each other whenever necessary for the purpose of carrying out their respective responsibilities under this Directive. Competent authorities shall render assistance to competent authorities in other Member States. Competent authorities shall respect the principle of home-country regulation and oversight by the Member State in which the statutory auditor or audit firm is approved and the audited entity has its registered office (Article 34(1) of the Directive).

It is helpful to distinguish between the characteristics of “inspections” and those of “investigations” in order to identify the scope of Article 36 of the Directive. Inspections, which in general take place on a regular basis, should contribute to enhancing audit quality in an inspected statutory auditor or an audit firm and should be principally of a preventative nature. They should aim at building and maintaining confidence in statutory audits and thus ultimately in financial markets. Investigations cover circumstances where there is suspicion of infringement or possible violation of laws, rules or regulations.

The following general conditions should apply to the exchange of information in the case of both investigations and inspections:

- (1) The receiving competent authority should explain the purpose of the request.
- (2) The information requested should be necessary and proportionate for this purpose and not obtainable otherwise. In other words, there is a need to know. A competent authority that can obtain information in other ways, for example from the group auditor in the member state of the receiving competent authority (in the case where the group auditor already has the requested information) should not request the information from the competent authority of another Member State.

The receiving competent authority should establish the need for the request. Once this need has been established, the transferring competent authority should transfer the requested information to the receiving competent authority **without questioning the relevance of the request**.

- (3) The information must relate to the carrying-out of statutory audits in the transferring Member State.
- (4) According to Article 36(4) of the Directive the transferring competent authority may refuse to act on a request for information where:
 - (a) supplying information might adversely affect the sovereignty, security or public order of the requested Member State or breach national security rules; or
 - (b) judicial proceedings have already been initiated in respect of the same actions and against the same statutory auditors or audit firms before the authorities of the requested Member State; or

- (c) final judgment has already been passed in respect of the same actions and on the same statutory auditors or audit firms by the competent authorities of the requested Member State.

The above conditions are necessary in order to minimise cases where competent authorities are faced with:

- (1) requests by competent authorities of other Member States where there is no need to know or the relevant information can be obtained otherwise;
- (2) unnecessary or disproportionate burdens on their capacity.

6.2. Cooperation in inspections

The Directive requires competent authorities in Member States to inform each other in the following instances:

- (1) Where a competent authority concludes that activities contrary to the provisions of the Directive are being or have been carried out on the territory of another Member State. The competent authority shall notify the competent authority of the other Member State of that conclusion in as specific a manner as possible. The competent authority of the other Member State shall take appropriate action. It shall inform the notifying competent authority of the outcome and, to the extent possible, of significant interim developments. (Article 36(5) of the Directive).
- (2) Where the approval of a statutory auditor or of an audit firm is withdrawn for any reason, the competent authority of the Member State where the approval is withdrawn shall communicate that fact and the reasons for the withdrawal to the relevant competent authorities of Member States where the statutory auditor or audit firm is also approved which are entered in the first-named Member State's register in accordance with Article 16(1) point (c).

In order to further develop effective cooperation, to the extent permitted by their respective national laws and procedures and without prior request, a competent authority should supply to competent authorities in other Member States any relevant factual information available to them and which they believe to be helpful to the other competent authorities for the purposes referred to in Article 36 (1) of the Directive. This may be considered in the following instances:

- (1) Disciplinary or criminal proceedings have been initiated against a statutory auditor with a registration with a competent authority in another Member State.
- (2) Administrative or criminal proceedings have been initiated against an audit firm with a registration with a competent authority in another Member State.
- (3) (Public) sanctions have been imposed against an audit firm and/or individual auditors with a registration with the competent authority in another Member State.

In addition, competent authorities could consider providing relevant factual information that relates to auditors/audit firms of a public interest entities (PIE) with a listing in another Member State.

The competent authorities in the transferring Member States should meet the requests for information within a reasonable period of time, preferably not exceeding a period of one month. If the transferring competent authority is not able to supply the required information within one month, it shall notify the receiving competent authority when the information will be available.

Finally, competent authorities of the Member States should strive to develop a common approach **and seek to** coordinate inspections of the firm-wide aspects of merger structures such as KPMG Europe LLP, Ernst & Young EMEIA or similar structures in the future.

6.3. Cooperation in investigations

According to Article 36(1) of the Directive competent authorities shall exchange information and cooperate in investigations related to the carrying-out of statutory audits. For this purpose competent authorities shall, on request, and without undue delay, supply any information required (Article 36(4) of the Directive).

The information is only to be used by the receiving competent authority for the exercise of its functions within the scope of the Directive and in the context of administrative or judicial proceedings specifically related to the exercise of those functions, without prejudice to the obligations to which it is subject in judicial proceedings (Article 36(4) of the Directive).

In addition to the requirements that apply to requests for information in general (see “general” above) the transferring competent authority is obliged to supply the information relating to investigations without undue delay. If the transferring competent authority is not able to supply the required information without undue delay, it shall notify the receiving competent authority of the reasons therefore (Article 36(4) of the Directive).

According to Article 36(6) of the Directive a competent authority of one Member State may also request that an investigation be carried out by the competent authority of another Member State on the latter's territory. It may further request that some of its own personnel be allowed to accompany the personnel of the competent authority of that other Member State in the course of the investigation. The investigation shall be subject throughout to the overall control of the Member State on whose territory it is conducted. Therefore the transferring competent authority should have full discretion regarding the extent and the manner in which assistance is provided.

The purpose of the requested assistance by a competent authority in one Member State should be an investigation to detect, correct and prevent inadequate execution of a statutory audit in the transferring Member State (Article 30(1) Directive).

Given the provision of Article 36(1) (“*In particular, competent authorities shall...cooperate in investigations...*”) there is an obligation – and not a discretion – to provide assistance in relation to an investigation on behalf of the receiving competent authority. The transferring competent authority may refuse assistance only in the cases mentioned under Article 36(6) of the Directive:

- (1) such an investigation might adversely affect the sovereignty, security or public order of the requested Member State; or
- (2) judicial proceedings have already been initiated in respect of the same actions and against the same persons before the authorities of the requested Member State; or
- (3) final judgment has already been passed in respect of the same actions on such persons by the competent authorities of the requested Member State.

7. TRANSFER OF RECEIVED INFORMATION TO OTHER MEMBER STATES

Information that has been transferred by one Member State (A) to another Member State (B) may only be transferred by the receiving Member State (B) to another Member State (C), with the consent of Member State A.

Example

Member State (A) transfers information concerning the audit of a subsidiary company to Member State (B), where the audit of the intermediate holding company takes place. Member State (C), where the audit of the parent company takes place, requests aggregated information from Member State (B) concerning the audit of both the subsidiary and intermediate holding company.

In general, however, it would be preferable that Member State (C) should request any information directly from Member State (A), as the original source, rather than through Member State (B), as an intermediary.

This procedure respects:

- (1) The principle of home-country regulation and oversight by the Member State in which the statutory auditor or audit firm is approved and the audited entity has its registered office.
- (2) The purpose for which the information was initially transferred by the competent authority of a Member State.

8. TRANSFER OF RECEIVED INFORMATION TO THIRD COUNTRIES

Information sent by a competent authority in one Member State (A) to a competent authority in another Member State (B) may not be transferred by the receiving Member State (B) to competent authorities in third countries. Competent authorities in third countries should direct their request to the competent authority in the Member State (A) that owns the information. This is necessary to respect the requirements of Article 47 of the Directive, which could otherwise be circumvented.

Example: The AFM in the Netherlands has no working arrangements with the competent authorities in Bermuda, unlike the AOC in Germany. If the AFM transfers information to the AOC and the AOC transfers that information to the competent authorities in Bermuda (even with the consent of the AFM), then the requirements of Article 47 of the Directive will not have been met.

ANNEX: LEGAL FRAMEWORK

The cooperation between EU competent authorities is subject to the following legal framework:

Article 34 of the Directive 2006/43/EC:

Mutual recognition of regulatory arrangements between Member States

1. Regulatory arrangements of Member States shall respect the principle of home-country regulation and oversight by the Member State in which the statutory auditor or audit firm is approved and the audited entity has its registered office.

Article 36 of the Directive 2006/43/EC:

Professional secrecy and regulatory cooperation between Member States

1. The competent authorities of Member States responsible for approval, registration, quality assurance, inspection and discipline shall cooperate with each other whenever necessary for the purpose of carrying out their respective responsibilities under this Directive. The competent authorities in a Member State responsible for approval, registration, quality assurance, inspection and discipline shall render assistance to competent authorities in other Member States. In particular, competent authorities shall exchange information and cooperate in investigations related to the carrying-out of statutory audits.

2. The obligation of professional secrecy shall apply to all persons who are employed or who have been employed by competent authorities. Information covered by professional secrecy may not be disclosed to any other person or authority except by virtue of the laws, regulations or administrative procedures of a Member State.

3. Paragraph 2 shall not prevent competent authorities from exchanging confidential information. Information thus exchanged shall be covered by the obligation of professional secrecy, to which persons employed or formerly employed by competent authorities are subject.

4. Competent authorities shall, on request, and without undue delay, supply any information required for the purpose referred to in paragraph 1. Where necessary, the competent authorities receiving any such request shall, without undue delay, take the necessary measures to gather the required information. Information thus supplied shall be covered by the obligation of professional secrecy to which the persons employed or formerly employed by the competent authorities that received the information are subject.

If the transferring competent authority is not able to supply the required information without undue delay, it shall notify the receiving competent authority of the reasons therefore.

The competent authorities may refuse to act on a request for information where:

(a) supplying information might adversely affect the sovereignty, security or public order of the requested Member State or breach national security rules; or

(b) judicial proceedings have already been initiated in respect of the same actions and against the same statutory auditors or audit firms before the authorities of the requested

Member State; or

(c) final judgment has already been passed in respect of the same actions and on the same statutory auditors or audit firms by the competent authorities of the requested Member State.

Without prejudice to the obligations to which they are subject in judicial proceedings, competent authorities which receive information pursuant to paragraph 1 may use it only for the exercise of their functions within the scope of this Directive and in the context of administrative or judicial proceedings specifically related to the exercise of those functions.

5. Where a competent authority concludes that activities contrary to the provisions of this Directive are being or have been carried out on the territory of another Member State, it shall notify the competent authority of the other Member State of that conclusion in as specific a manner as possible. The competent authority of the other Member State shall take appropriate action. It shall inform the notifying competent authority of the outcome and, to the extent possible, of significant interim developments.

6. A competent authority of one Member State may also request that an investigation be carried out by the competent authority of another Member State on the latter's territory. It may further request that some of its own personnel be allowed to accompany the personnel of the competent authority of that other Member State in the course of the investigation. The investigation shall be subject throughout to the overall control of the Member State on whose territory it is conducted.

The competent authorities may refuse to act on a request for an investigation to be carried out as provided for in the first subparagraph, or on a request for its personnel to be accompanied by personnel of a competent authority of another Member State as provided for in the second subparagraph, where:

(a) such an investigation might adversely affect the sovereignty, security or public order of the requested Member State; or

(b) judicial proceedings have already been initiated in respect of the same actions and against the same persons before the authorities of the requested Member State; or

(c) final judgment has already been passed in respect of the same actions on such persons by the competent authorities of the requested Member State.

7. In accordance with the procedure referred to in Article 48(2) the Commission may adopt implementing measures in order to facilitate cooperation between competent authorities on the procedures for the exchange of information and modalities for cross-border investigations provided for in paragraphs 2 to 4 of this Article.