



COMMENTS REGARDING MINISTRY OF FINANCE MEMORANDUM DS 2012:4 ON AUDITING IN FINANCIAL COMPANIES

The Swedish Corporate Governance Board was invited to comment on this memorandum and would like to submit the following opinions.

1 SUMMARY

Against the background of changes in EU Directives on auditing and auditors, new rules for stock exchange listed companies regarding areas such as auditor rotation and audit committees were introduced through the Swedish Companies Act in 2009. When implementing the rules, Sweden chose to utilise the possibility provided by the Directive to restrict the application of these rules to listed companies only. The Directive was also intended to regulate financial companies.

This memorandum proposes that the rules introduced for listed companies also be made applicable to financial companies. In addition to rules regarding auditor rotation and audit committees, the memorandum proposes that company boards, based on the recommendations of their audit committees, make decisions on to what extent the company may buy other services from the company auditor. This proposal does not correspond to any existing rule for listed companies.

On 30 November 2011, the European Commission proposed changes to its Audit Directive and new auditing regulations,¹ based on the Green Paper on audits and auditors that was presented on 13 October 2010.² The proposed audit regulations contain rules regarding auditor rotation, audit committees and using company auditors for services other than auditing. The proposals in the draft regulation on audits have, however, not been commented upon in the memorandum.

In view of the fact that new rules for financial companies can be anticipated in the areas covered by the memorandum, the Swedish Corporate Governance Board opposes the proposed rule changes.

2 AUDITOR ROTATION

For financial companies whose transferable securities are not traded on a regulated market, there is currently no requirement concerning auditor rotation. The memorandum proposes a maximum term of seven years for company auditors. If an audit firm is appointed, the rotation requirement applies to the chief auditor.

The fact that new rotation rules, with a completely different content than those proposed here, are highly likely to be introduced through the proposed audit regulations is a powerful argument against this proposal. In this proposal, the rotation requirement will be extended to cover not just the chief auditor in cases where audit firms are used, but also require the audit firm to be changed regularly. The proposal only allows an auditor to be reappointed once, and the term of office of an auditor may be no more than three years, (providing the company has not appointed several audit firms). The maximum term for an auditor would therefore be six years.

The introduction of new rules concerning rotation, which by nature are long term, for just a short time until the proposed audit regulations come into force, (either in their existing version or a revised form) is only likely to cause confusion among the companies concern and to impose costs on them. As the existing rules do not give rise to any particular problems, or at least none that are raised in the memorandum, there is no reason to introduce such rules at this time.

¹ See Proposal for a European Parliament and Council Directive amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts, COM (2011) 778 Final and Proposal for a European Parliament and Council Regulation laying down specific requirements for statutory audits of public interest, COM (2011) 779 Final.

² Audit Policy – Lessons from the Crisis, COM(2010) 561 Final.

3 AUDIT COMMITTEES

As with rotation, the memorandum proposes the introduction of a requirement equivalent to that which applies to listed companies for financial companies to have audit committees. There are several objections to the introduction of a requirement for non-listed companies to have audit committees.

New rules concerning audit committees are contained in the European Commission's proposed regulation on statutory audits. For the same reasons as those outlined above regarding rotation rules, there is no reason to introduce rules on audit committees that will only be applicable for a short time until the EU regulations, (either in their current form or a revised version), come into force. This is especially true in light of the fact that no particular problems have been found in this area.

Additionally, the rules concerning audit committees in listed companies are supplemented by the rules contained in the Swedish Corporate Governance Code, which were submitted in the background to the change in the legislation, (see Bill 2008/09:135, p. 114). For example, the Act does not define what is meant by the term "independent", as this is regulated by the Code. However, the Code is only applicable to listed companies, which means that those financial companies that are covered by the new audit committee rules will find no guidance in the Code.

Finally, objections can be raised against the requirement that at least one member of the audit committee is to have accounting or auditing competence. As the audit committee is made up of members of the company's board, this then becomes a requirement regarding the composition of the board. The same applies in cases where the whole board performs the task of the audit committee. The Swedish Corporate Governance Board is already deeply sceptical towards the existing rule for listed companies contained in the Companies Act, as the board of a Swedish listed company has collective responsibility for board decisions. Focusing on certain board members may lead to increased responsibility for these individuals (and reduced responsibility for others) on these issues, which conflicts with the traditions of Swedish company law. The model that should be used instead is a statement that the board as a whole should possess the competence required to handle these issues.

4 NON-AUDIT SERVICES

Finally, the memorandum includes a proposal that the purchase of services other than auditing from the company auditor requires approval by the company board. If the company has an audit committee, the board must await the committee's recommendation before making its decision.

No equivalent regulation exists for listed companies. Previously, the Swedish Corporate governance Code contained a similar rule which did not prescribe any prohibition or requirement concerning board approval. Furthermore, the Code rule was only an expression of good practice, which could be deviated from according to the comply or explain principle.

The rule proposed here is very brief. The services covered by the definition "audit services" are not defined. A similar but much more detailed rule is included in the European Commission's proposed audit regulations, and Sweden should therefore, also in this area, wait for the introduction of these regulations.

Stockholm, 14 May 2012

THE SWEDISH CORPORATE GOVERNANCE BOARD

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