



## COMMENTS REGARDING THE EUROPEAN COMMISSION PROPOSALS ON AUDITOR REGULATION AND CHANGES TO THE DIRECTIVE ON STATUTORY AUDITS AND CONSOLIDATED ACCOUNTS

The Swedish Corporate Governance Board, (“**the Board**”), has been invited by the Ministry of Justice to comment on the European Commission’s proposals concerning auditors and auditing. The new package contains proposals regarding a revised directive, COM(2011) 778, (“**the Proposed Directive**”), and a new regulation, COM(2011) 779, (“**the Proposed Regulation**”).

The Board has limited its comments to proposals regarding stock exchange listed companies, see proposed Article 1.2.d of the Proposed Directive, (“a. entities governed by the law of a Member State whose transferable securities are admitted to trading on a regulated market of any Member State...”). The Commission’s proposals regarding such companies are to be found in the Proposed Regulation.

Further, the Board has limited its comments to two issues, namely whether implementation of the Proposed Regulation would affect the Swedish corporate governance model and whether there is a need for the rules proposed. On all other matters, the Board is in agreement with views expressed in the comments submitted by the Confederation of Swedish Enterprise.

### 1 The role of the auditor in the Swedish corporate governance model

In the Swedish corporate governance model, the auditor is appointed by the shareholders’ meeting to examine on behalf of the shareholders and to report back to them how the directors, i.e. the board and the Chief Executive Officer, have run the company and to analyse the company’s accounts. Auditing and reporting which fulfils the shareholders’ requirements for greater confidence in financial reporting also meets the interests of other stakeholders in the company. Additionally, legislation and other regulations require auditors specifically to report openly to the general public on certain issues.

The point of departure of the Proposed Regulation, however, is not the same. According to recital (1) of the Proposal, auditors “are entrusted by law...with a view to enhancing the degree of confidence of the public” in the audited company, which means that auditors and audit firms “fulfil a particularly important societal role”. By this definition, auditors and audit firms are no longer representatives of the owners, but of society, which is an extremely far-reaching change. Further, recital (7) states that auditors are “a statutory safeguard for investors, lenders and business counterparties who have a stake or a business interest” in the audited company.

No analysis of this major revision is presented by the Commission. Such an analysis should have the role of the shareholder as its point of departure. One consequence of the Proposed Regulation is the risk of weakening the shareholders' engagement with and responsibility for the company. In the context of this revised role, auditors and audit firms will have significantly greater responsibility and will be an obvious responsible entity for every identified error in the accounts or should the audited company encounter financial difficulties. There is also the risk that this will lead to reduced liability for company boards and executive management teams. Furthermore, the increased involvement of the state in the appointment and monitoring of auditors means that the government will have to assume responsibility for failures. For example, according to Article 32.10 of the Proposed Regulation, the European Union's supervisory authorities are to issue guidelines on criteria governing the selection of auditors. It is the opinion of the Board that a company's choice of auditor should be the responsibility of the owners.

Another change to the corporate governance model is the proposals concerning audit committees. Article 31.1, paragraph 2 of the Proposed Regulation states that at least one member of the audit committee is to have competence in auditing, and that another member is to have competence in accounting and/or auditing. This is a stronger requirement than the one that exists today. According to Chapter 49a of the Swedish Companies Act, (2005:551), at least one member of the committee is to have competence in accounting or auditing. As the audit committee is composed of members of the company board, this becomes a requirement on the composition of the board. The same applies in cases where the whole board serves as the audit committee.

The Swedish Corporate Governance Board is already sceptical about the existing rule, as the board of a Swedish limited company is collectively responsible for the board's decisions. Identifying certain members may lead to greater responsibility for these individuals, (and less responsibility for the others), in these matters, which is in contradiction of the traditions of Swedish corporate legislation. A preferable model would be to state that the board as a whole is to possess the required competence in these issues.

Furthermore, this rule restricts shareholder freedom on the issue of composition of the board, not least with regard to other important criteria, such as diversity and breadth. The competence and experience required on boards varies from company to company, depending on its business, complexity, size etc. The Commission presents no analysis of whether an additional board member with competence in accounting or auditing would be beneficial to the company, its shareholders and society as a whole.

## 2 The need for regulation versus the costs

The Proposed Regulation, with all of its new requirements on both the companies to be audited and the auditors, will lead to significant increases in costs for listed companies. The Commission has not investigated the scale these costs, nor has the Commission shown that the revised rules will create value for the companies or for society that would justify them. In its analysis of the material presented by the Commission, the Board is unable to find any support for the need for the comprehensive changes proposed for the listed companies of Europe. The problems described refer to the financial sector.

Against the background of the above, the Board rejects the Proposed Regulation in its entirety. The Proposal should be returned to the Commission in order to be supplemented by a thorough impact assessment and cost analysis.

Stockholm, 20 January 2012

The Swedish Corporate Governance Board

Hans Dalborg  
Chair of the Board

Björn Kristiansson  
Executive Director