

# CONSULTATION PAPER

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## Consultation on Review of Mandatory Audit Firm Rotation for Local Banks

MAS

Monetary Authority of Singapore

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## 1 Preface

1.1 Pursuant to MAS Notice 615 on Appointment and Rotation of Auditors (“MAS Notice 615”), banks incorporated in Singapore shall not appoint the same audit firm for more than five consecutive years, except with the prior written approval of MAS. This requirement was temporarily suspended in October 2008 in view of the global financial crisis. MAS has since undertaken a review and is seeking public feedback on policy proposals on the appointment and rotation of auditors. Please refer to Annex A for the list of questions for public feedback.

1.2 MAS invites interested parties to provide their views and comments on the policy proposals in this paper.

**Please note that all feedback received will be published and attributed to the respective respondents unless they expressly request MAS not to do so. As such, if respondents would like (i) their whole submission or part of it, or (ii) their identity, or both, to be kept confidential, please expressly state so in the submission to MAS. In addition, MAS reserves the right not to publish any submission received where MAS considers it not in the public interest to do so, such as where the submission appears to be libellous or offensive.**

1.3 Please submit written comments by 31 October 2016 to –

Banking Department I  
Monetary Authority of Singapore  
10 Shenton Way, MAS Building  
Singapore 079117  
Fax: (65) 62203973  
Email: [auditorrotation@mas.gov.sg](mailto:auditorrotation@mas.gov.sg)

1.4 Electronic submission is encouraged. We would appreciate it if you use the suggested format for your submission to ease our collation efforts. You can access the template [here](#).

## **2 Introduction**

2.1 Under MAS Notice 615, banks incorporated in Singapore shall not appoint the same audit firm for more than five consecutive years, except with the prior written approval of MAS (“5-year audit firm rotation”). The requirement for mandatory audit firm rotation was first introduced in 2001 to enhance the independence and quality of external audits, and to avoid over-reliance on a single audit firm undertaking the audit of all local banks at any one time. This policy has been successful in reducing the concentration of local bank audits in a single firm and has also encouraged the building up of banking audit expertise in the audit industry.

2.2 The requirement for mandatory audit firm rotation was temporarily suspended in October 2008. During the period of unprecedented stress in the global financial market, banks were devoting substantial amount of time and resources towards heightened vigilance. MAS believed that the local banks<sup>1</sup> could benefit from audit continuity during the crisis through minimising any disruption that could arise when appointing a new audit firm. Since then, there have been regulatory developments to reinforce the need for improvements and attention over external audit quality and independence.

2.3 MAS has undertaken a review, taking into consideration the experience and feedback from the local banks and audit firms since the 5-year audit firm rotation was introduced in 2001, and regulatory developments since 2008. MAS proposes to discontinue mandatory audit firm rotation. The revised approach underscores the primary responsibility of local banks’ audit committees in ensuring the independence, objectivity and high quality of external audit. At the same time, MAS proposes to introduce a requirement for re-tendering of audit engagements every 10 years.

## **3 Proposed revisions**

### Discontinuation of mandatory audit firm rotation

3.1 The global financial crisis in 2008 has heightened attention internationally on the quality of external audits of banks and auditor independence. Reviews performed in recent years by various jurisdictions on the proposal for mandatory firm rotation, however, yielded mixed results. For instance, the United States House of Representatives passed a bill to prohibit the Public Company Accounting Oversight Board from imposing

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<sup>1</sup> These refer to DBS Bank Ltd, United Overseas Bank Ltd and Oversea-Chinese Banking Corporation Ltd.

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mandatory audit firm rotation on public companies. The Chartered Professional Accountants of Canada and Canadian Public Accountability Board jointly performed a review and concluded that mandatory rotation would not contribute to the enhancement of audit quality. On the other hand, the European Union introduced a requirement for mandatory rotation of audit firms of public interest entities.

3.2 Domestically, additional safeguards have been introduced since 2008 to enhance the independence and quality of audits. These include the reinforcement of MAS' expectations to audit committees ("ACs") of local banks to ensure independence, objectivity and high quality of external audit in MAS' Guidelines on Corporate Governance (the "CG Guidelines") in 2013, the provision of additional guidance to the ACs in the evaluation of auditor re-appointments in the revised Guidebook for ACs (the "Guidebook") in 2014 and the widening of the scope of partner rotation and cooling off requirements to include "Key Audit Partners"<sup>2</sup> in the revised Code of Professional Conduct and Ethics for Public Accountants and Accounting Entities in 2015. MAS has also highlighted to the external auditors<sup>3</sup> its supervisory expectations for audits of banks, with reference to the supervisory guidance on "External Audits of Banks" issued by the Basel Committee on Banking Supervision in 2014.

3.3 The intent of mandatory audit firm rotation is to reduce familiarity threats arising from the long association of audit firms with an audit client, and ultimately leading to higher audit quality. However, research studies conducted thus far internationally did not provide conclusive evidence linking mandatory firm rotation with an improvement in audit quality. From MAS' observations and feedback received from stakeholders, MAS recognises that there are also negative consequences associated with frequent rotation of external auditors. Specifically, external auditors take time to gain familiarity with the bank given the size and complexity of the local banks' business activities, and the loss of cumulative audit knowledge following an audit firm rotation could lead to poorer audit quality and heightened audit risks in the early years of appointment.

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<sup>2</sup> "Key Audit Partner" is defined as the engagement partner, the individual responsible for the engagement quality control review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, "other audit partners" may include, for example, audit partners responsible for significant subsidiaries or divisions.

<sup>3</sup> For avoidance of doubt, the term "external auditors" as used in this document refers to the audit firm and not the individual engagement partner.

3.4 The regulatory developments since 2008 as mentioned above have accorded greater focus and attention over external audit quality and independence. In addition, the ACs continue to be primarily responsible in evaluating the effectiveness of external auditors and recommending for approval their appointment or re-appointment on an annual basis. On balance, taking these into consideration and the potential risk of audit gaps arising from frequent change of auditors, MAS proposes to discontinue mandatory audit firm rotation.

**Question 1.** MAS seeks comments on the proposed discontinuation of the mandatory audit firm rotation for local banks.

### Mandatory audit re-tendering

3.5 In view of the proposed discontinuation of mandatory audit firm rotation, MAS proposes to implement mandatory audit re-tendering as a compensating safeguard to mitigate risks arising from potential erosion of audit independence. A tendering exercise provides an opportunity for banks and their ACs to periodically assess and compare, in a more formal manner, the quality and effectiveness of the services provided by their incumbent auditors with those of other audit firms. A tendering exercise also increases transparency and openness in the award of audit mandates.

3.6 MAS recognises that frequent re-tendering of external auditors can be costly and time-consuming, and if not properly implemented, could be reduced to a box-ticking exercise. There are also risks that banks may be overly focused on audit fees rather than audit quality during a tendering exercise.

3.7 MAS is of the view that requiring local banks to perform a re-tendering exercise every ten years provides an appropriate balance. As stipulated in the CG Guidelines, MAS expects ACs of local banks to have robust processes to discharge their responsibilities in recommending for approval the appointment, reappointment, removal and remuneration of the external auditor, during a tendering exercise or otherwise. MAS also expects the ACs to determine appropriate criteria for selecting the external auditor. In this regard, the ACs should consider the guidance provided in the Guidebook.

3.8 ACs of the local banks have an important role in ensuring the independence, objectivity and quality of external audit of the banks. The ACs must continue to maintain adequate oversight and have in place a robust process to regularly monitor and assess the knowledge, competence, independence and effectiveness of external audit.

**Question 2.** MAS seeks comments on the proposed requirement for local banks to conduct a mandatory audit re-tendering exercise every ten years.

## **4 Existing policies and other considerations**

4.1 For clarity, local banks' appointment of external auditors will continue to be subject to MAS' supervisory assessment and approval annually. MAS will also retain the requirement that no single audit firm is allowed to undertake the audit of all local banks at any one time. This is to avoid over-reliance on a single audit firm.

4.2 In addition, audit partners continue to be subject to the rotation and cooling-off requirements stipulated in the SGX Listing Rules and Code of Professional Conduct and Ethics for Public Accountants and Accounting Entities.

4.3 MAS has also considered but decided against requiring external auditors to establish an internal rotation policy for the periodic renewal of audit managers and staff at working level. This is in recognition of the operational difficulties in institutionalising such a policy and that the natural attrition generally experienced by audit firms could reduce the familiarity threats to some extent.

## **5 Implementation**

MAS will evaluate the views and comments received in determining the final revisions to MAS Notice 615. Based on the proposed tendering period of ten years, banks with incumbent auditors in place for ten consecutive years or more will be required to perform a re-tendering exercise for an audit firm to carry out the duties specified in section 58 of the Banking Act for the financial year ending 31 December 2018. Banks with incumbent auditors in place for eight or nine consecutive years will be required to perform a re-tendering exercise for an audit firm to carry out the duties specified in section 58 of the Banking Act for the financial year ending 31 December 2020.

<b>Question 3.</b> MAS seeks comments on the proposed implementation timelines.
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**Annex A**

**LIST OF QUESTIONS**

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