

Guidance on scope of the legislation and Public Interest Entities (PIEs)

General application

This paper sets out our latest guidance on the EU audit legislation, which was adopted in April 2014 by the EU institutions. The legislation entered into force on 16 June 2014 and its provisions will be applicable to the first financial year starting on or after 17 June 2016, with the exception of mandatory firm rotation, which is subject to transitional arrangements.

The legislation comprises two legislative instruments. The Directive, which needs to be transposed into national law, applies to all entities required to have a statutory audit. The Regulation, which is binding on all EU member states, introduces further requirements for Public Interest Entities (PIEs) in the EU.

Summary of scope of the adopted legislation regarding the definition of PIEs

Below is a summary of the definition of those entities which are classified as a PIE in the EU legislation.

Public Interest Entities
<ul style="list-style-type: none"> • All entities that are both governed by the law of a member state and listed on an EU regulated market
<ul style="list-style-type: none"> • All credit institutions in the EU, irrespective of whether listed or not
<ul style="list-style-type: none"> • All insurance undertakings in the EU, regardless of whether they are listed or not and regardless of whether they are life, non-life, insurance or reinsurance undertakings
<ul style="list-style-type: none"> • Entities designated by member states as public-interest entities, for instance undertakings that are of significant public relevance because of the nature of their business, their size, or number of employees

The PIE concept is not a new one. The 2006 Statutory Audit Directive (the 8th Directive) included the same definition.

The impact of having an EU PIE in a group

The Regulation applies to individual entities. If an individual entity qualifies as a PIE, the Regulation will apply to that PIE irrespective of whether its parent company is a PIE or not, and irrespective of whether its parent is outside the EU or not.

However, the NAS prohibitions, the NAS fee cap and the requirement for Audit Committee approval will also impact parent undertakings and controlled undertakings of the PIE, with some territorial limitations.

These Guidance/Q&As reflect frequent questions received from audit professionals and from clients. They are designed to help understand and apply the EU audit legislation in a consistent manner, drawing on the European Commission's Q&As regarding the audit Regulation and Directive. The content is provisional, updated on a regular basis and no representation or warranty (express or implied) is given as to the accuracy or completeness of it. These Guidance/Q&As have been prepared to provide general guidance on matters of interest only, and do not constitute professional advice. You should not act upon the information contained herein without obtaining specific professional advice. To the extent permitted by law, PwC does not accept or assume any liability, responsibility or duty of care for any consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this document or for any decision based on it. PwC refers to the PwC network and/or one or more of its member firms, each of which is a separate legal entity. Please see [www.pwc.com/structure] for further details.

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Q&As on the scope of the legislation and PIEs:

Q: What exactly is the EU Audit legislation?

A: The EU Audit legislation consists of two pieces of EU law, the Directive 2014/56/EU and the Regulation 537/2014. The legislation entered into force on 17 June 2014 and became applicable on 17 June 2016. However, most requirements apply to financial years that start on or after 17 June 2016. In many cases these will be financial years starting 1 January 2017.

Q: What is the interrelationship between the requirements in the Directive and the Regulation?

A: The Directive applies to all statutory auditors/audit firms and their clients in the European Union, whereas the Regulation is only applicable to audits of public interest entities (PIE). While the Directive needs to be transposed into national law, the Regulation is directly applicable in each member state. However, due to various member state options in the Regulation, there will need to be national implementation of any options that a member state may wish to exercise.

Q: And what is the interrelationship between the independence requirements in the Directive and Article 5 of the Regulation?

A: The independence requirements under the Directive apply to all statutory auditors and audit firms, irrespective of whether they carry out the statutory audit of PIEs or not. Article 5 of the Regulation is an “extra rule” that contains additional prohibitions that apply to statutory auditors and audit firms which audit PIEs and concern their parent companies and controlled undertakings as well.

Q: My company is incorporated in Norway, but Norway is in the EEA, not the EU. Will the EU audit rules apply?

A: Yes, the non-EU countries in the EEA (i.e. Norway, Liechtenstein and Iceland) will adopt national legislation to implement the EU Audit legislation. This means that the law only comes into effect once implemented in the respective country. Before the entry into force of the Norwegian law (anticipated in 2018) compliance with the local independence rules in Norway will be required but not with the EU Audit legislation.

Q: What about Switzerland? Will the EU audit rules apply there?

A: No, Switzerland is neither part of the EU nor the EEA and has indicated that it will not implement rules like the EU Audit Regulation. Swiss companies will therefore only be affected by the EU Audit Regulation to the extent that they are controlled undertakings of a PIE as regards the services mentioned in Art. 5.5.

Q: I understand that one category of PIEs are entities governed by the law of a member state whose transferable securities are admitted to trading on a regulated market of any member state. What does 'governed by the law of an EU member state' mean?

A: We need to look at the local law of the relevant member state to assess the precise meaning of this phrase. That said, references to companies that are 'governed by the law of an EU member state' are generally understood to mean companies that are incorporated in that member state. So, companies incorporated outside the EU that are listed on a regulated market within the EU would not qualify as a company governed by the law of an EU member state.

Q: What happens if an EU entity is listed on an EU regulated market but has no securities actually traded on that market?

A: An entity (governed by the law of an EU member state) does not need to be actively traded on an EU regulated market to qualify as a PIE; it is enough that it is listed on a regulated market. This position is based on the definition of a PIE which mentions 'entities governed by the law of a member state' whose transferable securities are admitted to trading on a regulated market of any member state. This entity would only cease to be a PIE if it was to be delisted from the EU regulated market.

Q: I'm trying to work out if my company is an EU PIE - it's incorporated in France and has listed debt on a Luxembourg stock exchange. How do I check if the Luxembourg exchange is a regulated EU exchange?

A: You'll need to check the list of regulated EU exchanges which is published by the European Securities and Markets Authority (ESMA) and is periodically updated. Here's a link to the list:

http://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_mifid_rma

Q: Is a subsidiary of an EU PIE a PIE?

A: No, a subsidiary of a PIE is not necessarily a PIE in its own right. It will be a PIE if it is EU incorporated and has securities listed on a regulated EU exchange or is a credit institution or insurance undertaking itself.

Q: My company is a non-PIE entity in the UK, which has a subsidiary in the US, which in turn has a UK PIE subsidiary. Do the NAS prohibitions of the Regulation apply to the non-PIE entity in the UK?

A: Yes, the NAS prohibitions apply to the non-PIE entity in the UK. This is because the "parent undertaking" and "subsidiary undertaking" concepts cover not only direct parents and subsidiaries but also indirect parents and subsidiaries (i.e. undertakings which indirectly control or are indirectly controlled by another undertaking) and therefore the entire chain of ownership.

Q: Does a pension fund qualify as a PIE, under the new rules?

A: No, in principle a pension fund does not meet the definition of a PIE, however member states have the option to designate certain entities as a PIE if they are considered to have significant public relevance, e.g. because of the nature of their business, their size or number of employees, and these could include pension funds.

Q: Would a Barbados insurance company, listed on the London Stock Exchange qualify as an EU public interest entity?

A: If the Barbadian subsidiary is itself the recipient of a licence from an EU member state to act as an insurance company, then it becomes an "insurance undertaking" and hence a PIE for EU purposes. If the entity is a branch, the branch will not itself be the recipient of a licence itself; given it is part of a larger undertaking – i.e. branches don't have legal personality in themselves; any licence to act as an "insurance undertaking" in the EU would be given to the larger undertaking of which the branch forms a part.

Q: Would a Cayman fund (hedge fund for high net worth investors, minimum buy \$250k and convenience listing on Irish Stock Exchange) qualify as an EU public interest entity?

A: A fund listed on an EU regulated market but registered outside of the EU, would not be classed as a PIE as it is not 'governed by the law of an EU member state', assuming it does not meet one of the other PIE definitions (credit institution, insurance undertakings or other entities designated as PIEs by member states).

Q: My company is a US bank with branches in a number of EU member states. Will the bank's branches in the EU be subject to the requirements of the EU audit legislation?

A: Where a non-EU group has a branch in an EU member state, the branch is not an EU PIE for the purposes of the Regulation. Note that local law may be more restrictive and needs to be considered in addition.

Q: What if my company is a French bank with branches in other EU member states? Which non-audit services and rotation rules do the branches need to follow?

A: The branches are an indivisible part of the PIE they belong to, and they (and their auditors) would thus have to follow the French rules.