Audit partner rotation assignment

The 2003 rules on the topic of audit partner rotation states that an audit partner must be rotated off the audit engagement if he/she has worked (been responsible for the issuance of the audit report reflecting the reporting of the financial statements and the dealings with the audit committee and management) on the engagement for the prior five consecutive years and be subject to a five year " time-out period" from the registrant.

Previously, this rule was that the lead audit partner was to be rotated after seven years with a two year " time-out" period. Clearly, changes have been made and exceptions have been created as many concerns were brought up regarding this matter. When evaluating the 2003 rules regarding audit partner rotation, the main question that comes to mind is, are these rules fair? Will the benefits outweigh the changes that will need to be made in order to implement the new rule including the effect of the impact to the individual audit partners?

In order to apply the rule, there needs to be a way that it will be consistent and rational across the accounting profession considering all types and sizes of accounting firms. Therefore, the SEC came up with a few exceptions to alleviate this matter. First, being that " specialty" partners would be excluded from the five-year audit rotation requirement because they usually do not perform the same tasks or have the same responsibility as the lead audit partner. Secondly, the rule is excluded for partners who function as a technical resource for the audit.

These partners are used when the audit contains complex business transactions and the partner is responsible for dealing with the national

office. Since this partner does not primarily deal with the auditing of the financial statements they are not subject to the rotation requirements. Lastly, smaller accounting firms are at a disadvantage for this requirement because there are not enough partners to rotate. Therefore, the SEC made an exception for accounting firms that have less than five audit clients and less than ten partners.

Because these firms are excluded from the five-year audit partner rotation requirement, the SEC implemented a special rule requiring the PCAOB review the audit engagements of these firms at least once during a three year time period. This will ensure that the quality of their reports and competence of the partners are equivalent to that of the firms who are required to follow the five-year rotation requirement. There are significant advantages of the partner rotation requirements including uditor independence and the removal of continuity for better quality audit reports; however, some believe that the amount of negative aspects and concerns that the rotation brings to many in the audit profession outweigh the benefits. There are people that are apprehensive to the rule for a few reasons. One being that it is important to have expertise in a certain industry in order to accurately deliver a truthful audit report. This takes years of experience and it is at the lead audit partner level where you find this expertise and knowledge.

If the rule requires a five year rotation of these partners with this knowledge, then you lose the standard of quality that their reports once had. In turn this can affect investor perception of the audit report. Also, it takes time to gain industry knowledge at the start of an audit report so if there is continuous rotation then at the beginning of every five year rotation, fees will be high

and registrants will be upset. The last reason is that people argue this rotation requirement will negatively impact the audit partners " quality of life".

This requirement may cause partners to have to relocate. Subsequently, this may drive potential audit professionals out of the profession due to the uncertainty of the possibility of reassignment in the future. In conclusion, it boils down to if you believe that the benefit of producing a more accurate audit report is greater than some of the consequences that may come from the new requirement. If the rules are implemented fairly, which in my opinion with the additions of the exceptions they have been, then the five-year audit rotation requirement is necessary.

It all depends on the amount of involvement that the audit partner has in the audit engagements that determine if they are subject to the five year rotation rule. Ultimately, I agree with the five year rule and it should only be applied to lead auditing partners. As long as it is fair and consistent then I believe it will benefit the auditing practice. Going down the ladder and having the rule be applied to anyone else on the audit engagement is unnecessary and would be costly.

Implementing this rule will allow for better regulation of audits and also permit more accurate audit reports. The idea behind improved accuracy is that the rotation will eliminate redundancy and will provide a new aspect when auditing the financial statements. All things considered and providing that there are exceptions in place, I believe that the five-year rotation rule will be advantageous for both the accounting firms and the registrants.

Sources: http://aaahq. org/meetings/AUD2010/AuditPartnerRotation. pdf

http://www. sec. gov/rules/final/33-8183. htm