INDEPENDENCE RULES - LONG ASSOCIATION OF SENIOR PERSONNEL ON AUDIT ENGAGEMENTS

Author: Professional Advisory Services | June 2021

As a CPA practitioner conducting audits, it is important that you maintain your independence in long-lasting client relationships. To address familiarity threats caused by having the same senior personnel on an audit engagement over a long period, the CPA Code contains specific requirements and considerations depending on the type of client and the nature of your role.

Partner rotation rules for audit engagements

The CPA Code requires a change in certain senior personnel after a specified duration (maximum time-on period), followed by a period where they cannot participate in the audit engagement (minimum time-off period). The length of the minimum time-off period depends on the role you perform. The following independence rules relate to partner rotation on an audit of the financial statements of a reporting issuer or listed entity[1] (including mutual funds):

- You can perform the role of lead engagement partner[2] or engagement quality control reviewer[3] (EQCR) for up to seven years in total, after which you cannot participate in the audit for at least five years.[4]
- If you are a key audit partner[5] other than the lead engagement partner or EQCR, you may perform that role for up to seven years, after which you cannot participate in the audit for at least two years.[6]
- If you have already been a key audit partner for five or more years when an audit client becomes a reporting issuer or listed entity, you can continue in that role for up to two more years before being replaced.[7]

Relevant rules in the CPA Code of Professional Conduct (CPA Code):

- Rule 204, *Independence*
- Rule 204, *Definitions*
- Rule 204.4(20), *Long association of senior personnel with a reporting issuer or listed entity audit client*

1 “Reporting issuer” and “listed entity” are defined in Rule 204.4
2 “Lead engagement partner” means the partner or other person who is responsible for the engagement and its performance, for the report that is issued on behalf of the firm and who, where required, has the appropriate authority from a professional, legal or regulatory body.
3 “Engagement quality control reviewer”, often referred to as reviewing, concurring or second partner, means the audit partner or other person in the firm who, prior to issuance of the audit report, provides an objective evaluation of the significant judgments made and conclusions reached by the members of the engagement team in formulating the report on the engagement.
4 204.4(20)(a)
5 “Key audit partner” means: (a) an audit partner who is the lead engagement partner; (b) the engagement quality control reviewer; and (c) any other audit partner on the engagement team who makes important decisions or judgments on significant matters with respect to the audit or review engagement. A key audit partner does not include “specialty” and “technical” partners who consult with others on the engagement team regarding technical or industry-specific issues, transactions or events, including tax matters.
6 204.4(20)(b)
7 204.4(20)(c)

The table below summarizes the maximum time-on and minimum time-off periods for key audit partners:

Role	Maximum Time-On Period	Minimum Time-Off Period
Lead engagement partner	7 years	5 years
EQCR	7 years	5 years
Other key audit partners	7 years	2 years

Restricted services for reporting issuers or listed entities during the time-off period

During their respective minimum time-off periods, the lead engagement partner, EQCR and other key audit partner cannot:

- provide services directly related to the audit or to a review of interim financial statements,
- provide quality control for either such engagement,
- consult with the engagement team or the client regarding technical or industry-specific issues, transactions or events, or
- directly influence the outcome of any such engagement.[8]

Despite these restrictions, such partners may be consulted for transferring client knowledge to the engagement team.[9]

Evaluating the familiarity threat for senior personnel on the engagement team

The CPA Code does not specify the maximum time-on period for a key audit partner when the assurance client is not a reporting issuer or listed entity. If the engagement is lengthy, however, a familiarity threat may still arise for senior personnel. You and your engagement team should evaluate the significance of the potential threat and apply safeguards to reduce it to an acceptable level, unless it is clearly insignificant.

8 204.4(20), guidance paragraph 2
9 204.4(20), guidance paragraph 2

For example, if you have been the lead engagement partner on the audit of a private entity for ten years, you may want to ask another partner who has never been involved with the engagement to review your work or advise you as necessary. When acting as a key audit partner, familiarity threat factors to consider include:

- your role on the engagement team,
- the structure of your firm, and
- the nature of the assurance engagement, including the complexity of the subject matter and degree of professional judgment needed.

Safeguards to reduce a familiarity threat to an acceptable level might include:

- discussing the matter with the audit committee,
- replacing the senior personnel on the engagement team,
- subjecting your files or the firm to an external practice inspection, and
- having someone (within or outside your firm) who was never on the engagement review your work.[10]

Common scenarios related to partner rotation

Scenario 1
You perform audits and reviews for companies that are not reporting issuers or listed entities. Do the partner rotation requirements apply to you?

There are no specific partner rotation requirements in the CPA Code for clients who are not reporting issuers or listed entities. However, long-time association of senior personnel with an assurance client can still create a familiarity threat that should be evaluated. If the threat is significant, apply safeguards to reduce the threat to an acceptable level.

Scenario 2
After five years as lead engagement partner for a reporting issuer client, you rotated off for a year. Can you resume the role of either lead engagement partner or EQCR?

If you serve as lead engagement partner for less than seven years, you can take a break and resume your role as long as the cumulative total does not exceed seven years. Since you have served as lead engagement partner for five years in this scenario, you can resume this role or that of EQCR for a further two years, after which you must rotate off and cannot resume these roles for at least five years.

Year 1	Year 3	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8
Lead engagement partner	Lead engagement partner	Lead engagement partner	Lead engagement partner	Lead engagement partner	Not on engagement	Lead engagement partner or EQCR	Lead engagement partner or EQCR

10 204.4(20), guidance paragraph 1

Scenario 3

You have been the lead engagement partner on an audit since the 2014 year end. In fiscal 2017, the entity became a reporting issuer. Can you continue in your role as lead engagement partner and complete the audit for the 2020 year end?

When a client becomes a reporting issuer, you must consider the length of time you have served as lead engagement partner. If it is five years or more, you can continue for two more years before being replaced. In this scenario, since you served as lead engagement partner for less than five years when the entity became a reporting issuer in 2017, you would count the duration of your role, with 2014 being year one. Since 2020 is year seven, it is the last year in which you can serve as lead engagement partner before rotating off for five years.

Year 1 2014	Year 3 2015	Year 3 2016	Year 4 2017*	Year 5 2018	Year 6 2019	Year 7 2020
Lead engagement partner	Lead engagement partner	Lead engagement partner	Lead engagement partner	Lead engagement partner	Lead engagement partner	Lead engagement partner

*Company became a reporting issuer

Scenario 4

You have been the EQCR for a public company client since 2014 and it became a reporting issuer during fiscal 2020. Can you stay on to complete the 2021 audit?

When an audit client becomes a reporting issuer or listed entity, you can continue in the role of EQCR for two more years before being replaced, provided you have already been an EQCR for five or more years. In this scenario, although you would have been the EQCR for six years when the company became a reporting issuer during fiscal 2020, you could continue for two more fiscal years; 2020 and 2021 are years one and two respectively. You would then need to rotate off for five years before resuming the role of either EQCR or lead engagement partner.

Year 1 2014	Year 3 2015	Year 3 2016	Year 4 2017	Year 5 2018	Year 6 2019	Year 7 2020*	Year 8 2021
EQCR	EQCR	EQCR	EQCR	EQCR	EQCR	EQCR	EQCR

*Company became a reporting issuer

Scenario 5
Your client, Company A, is a private company and recently merged with a public company, Company B. You have been asked to continue as lead engagement partner of the new, combined public entity. When does the period for the determination of partner rotation begin?

Since Company A became a public entity once the merger transaction was complete, you must consider the duration of your role as lead engagement partner prior to the merger. If it is five years or more, you can continue in that role for two more fiscal years before being replaced. If it is less than five years, you can remain in that role for a maximum of seven years, including the number of years you performed this role for Company A prior to the merger.

Additional resources

For further information, the following resources may be helpful:

- CPA Guide to Canadian Independence Standard
- International Ethics Standards Board Staff Questions and Answers – Long Association of Personnel with an Audit Client (May 2019)

As no two situations are identical, you are responsible for ensuring that your own situation complies with the CPA Code of Professional Conduct, By-law and Regulations. Please note that this article is considered to be non-authoritative guidance only.