

Meeting: IESBA CAG
Meeting Location: New York
Meeting Date: September 9, 2019

Agenda Item

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Fees

Objectives of Agenda Item

1. To:
 - (a) Report back on the March 2019 IESBA CAG discussion; and
 - (b) Discuss key issues identified by the Task Force and to obtain Representatives' input on the proposed revisions to the fee-related provisions in the Code.

Project Status and Timeline

2. In September 2018, pursuant to the June 2018 final report of the Fees Working Group ([Fees Final Report](#)), the IESBA approved the [Fees Project Proposal](#). The objective of the project is to review the provisions in the [International Code of Ethics for Professional Accountants \(including the International Independence Standards\)](#) (the "Code") pertaining to fee-related matters.
3. The scope of the project encompasses the following specific areas:
 - A review of the provisions with respect to the level of audit fees for individual audit engagements, including the role of professional accountants in business (PAIBs) in approving the level of audit fees.
 - A review of the provisions pertaining to fee dependency at a firm, office and partner level for all audit clients, including considering the introduction of a specific threshold for audit clients which are not public interest entities (PIEs).
 - A review of the safeguards in the Code pertaining to the scope of this project.
4. In March 2019, the IESBA and the CAG first discussed the Task Force's [Proposals to Strengthen the Fee-related Provisions in the Code](#). In June 2019, IESBA was presented with the [Proposed Revisions to the Code Arising from the Fees Project](#) for "first read."
5. Based on the [Updated IESBA Project Timetable](#), with regard to the timeframe necessary to allow appropriate coordination with the IAASB on overlapping issues, the fees Exposure Draft (ED) is scheduled for approval in December 2019.

Report Back on March 2019 CAG Discussions

6. Appendix I includes a project history. At the March 2019 CAG meeting, Representatives expressed views on the Task Force's preliminary proposals to strengthen the fee-related provisions of the Code. In developing its updated proposals, the Task Force carefully considered the Representatives' suggestions.

7. Appendix II include extracts from the draft minutes of the March 2019 CAG meeting¹ and an indication of how the Task Force has responded to CAG Representatives' comments.

Coordination with the NAS Task Force and IAASB

Coordination with NAS Task Force

8. The Task Force has coordinated its efforts with the NAS Task Force to develop proposals relating to threats created by the ratio of audit fees and fees for services other than audit, and the enhanced transparency of such information.

Coordination with IAASB

9. Based on the issues identified and the proposals developed, in May 2019 the Task Force signaled the need to coordinate with the IAASB on a number of overlapping issues² with the requirements of International Auditing Standards (ISAs). As a follow up to several internal coordination discussions between IESBA and the IESBA staff and leadership, a Joint Working Group (JWG) comprising representatives of the IAASB and IESBA (including the Task Force Chair) has been established to facilitate the timely coordination of overlapping topics arising from the Fees Project.
10. The JWG has met first via teleconference in early June. The IAASB representatives provided their preliminary views and reactions to the Task Force's proposals, noting that their reactions represented their individual views and not the official IAASB view. The Task Force presented the IAASB representatives' views to the Board at its June meeting.
11. The JWG met for the second time via teleconference in August. The IAASB representatives on the JWG were provided with the preliminary proposals of the Task Force regarding enhanced transparency developed at the Task Force's meeting earlier in August. The IAASB representatives were generally supportive of the progress made in terms of the structure of the document, simplification of the provisions, and the greater focus on principles vs prescription. They appreciated the greater flexibility regarding the approach to public disclosure. The Task Force Chair will present the further feedback provided by the IAASB Representatives during the September 2019 CAG meeting.
12. The IAASB will consider the Task Force's proposals on overlapping issues for the first time at its September 2019 meeting. The Task Force Chair will also attend the IAASB session to provide any clarifications needed regarding the Task Force's thinking and direction of the proposals, and to listen to the IAASB discussion. The IESBA will be provided a report back on this discussion during the the September 2019 IESBA meeting

September 2019 IESBA Meeting

13. The IESBA will consider at its September 2019 meeting a presentation by the Task Force Chair setting

¹ The March 2019 CAG minutes will be approved during the September 2019 IESBA CAG meeting.

² Areas of the Fees Project that are overlapping with the requirements of ISAs are the following:

- (a) Responsibility of the firm and the engagement partner for fees and appropriate resources;
- (b) Communication of fee-related information to those charged with governance;
- (c) Disclosure of fee-related information in the auditor's report.

out the Task Force's key decisions/proposals. The Board will be asked for its views on the Task Force's approach, whether it supports those decisions and proposals.

14. IESBA members will be asked to consider and provide input particularly in relation to the following matters:
- (a) Does the Board agree with the Task Force that payment of fees by an audit client creates threats to independence and that the Code should make explicit reference thereto?
 - (b) Does the Board agree with the Task Force that the Code should address the level of the audit fee as a standalone matter, and that it should include provisions to address threats created by fees paid for the provision of services other than audit to the audit client?
 - (c) Does the Board agree with the Task Force that in the case of fee dependency, the Code should have different approaches for PIE and non-PIE clients, allowing greater flexibility in the approach for non-PIE clients?
 - (d) Does the Board agree with the Task Force that excessive fee dependency on a PIE audit client should not be permitted to continue indefinitely unless, exceptionally, it can be shown to be in the public interest to do so?
 - (e) Does the Board agree with the Task Force that transparency is an appropriate tool to mitigate threats created by fees paid to a PIE audit client and that the Code should include provisions to promote such transparency?
 - (f) The possible ways to achieve public disclosure of fee-related information, and how the Code could promote such disclosure.

Matters for CAG Consideration

15. At its September 2019 meeting, the CAG will receive a presentation summarizing the Task Force proposals and will be asked to:
- (a) Note the report back in **Appendix II**.
 - (b) Consider and provide comment on:
 - The key proposals highlighted in **Appendix III** of this paper; and
 - The matters that will be discussed by the Board in **paragraph 14** of this paper.
 - (c) Indicate whether they believe that all key issues set out in the Fees project proposal are being appropriately dealt with.
 - (d) Provide views about any other matters CAG Representatives believe should be dealt with in the Fees project.

Material Presented

Agenda Item F-1 Fees – Proposed Revisions to Part 4A (Clean)

Project History

Project: Fees

	CAG Meeting	IESBA Meeting
Information gathering/ Discussion	September 2018	June 2018
Approval of project proposal	September 2018	September 2018
Development of proposed international pronouncement (up to exposure)	March 2019	March 2019 June 2019

Report Back on March 2019 CAG Discussions

Matters Raised	Task Force/ IESBA Response
LEVEL OF AUDIT FEES	
<ul style="list-style-type: none"> • Mr. James asked how to assess that auditors are determining the appropriate fee level for the resources needed. He wondered whether there is a need for more granularity in the proposals (e.g. in terms of audit hours or other objective parameters). • Mr. Yurdakul was of the view that enforcement of the requirement relating to the engagement partner would be difficult. He asked whether there should be some sort of reasonable and informed third party test or use of industry benchmarks. 	<p>Mr. McPhee responded that the Task Force is relying on transparency (supported by application material). He was of the view that it would be complicated to take a more granular approach as there are many variables in play. For example, some NAS such as a review of internal control may facilitate a more efficient audit process. Accordingly, he felt it best to see how the market would respond to the new requirements and for the IESBA to undertake an implementation review in due course.</p> <p>The Task Force has strengthened the link to independence and the current proposed requirement regarding level of fees focuses on the firm's independence and hence its ability to perform the audit in compliance with the fundamental principles, including in accordance with professional standards.</p> <p>See proposed <i>paragraph R410.4</i> in Agenda Item F1.</p>
<ul style="list-style-type: none"> • Mr. van der Ende supported the Task Force's approach focusing on the resources needed and not on the amount of fees. He noted that the Basel Committee's guidelines relating to the external audit of banks focus on the resources for the audit and encourage TCWG to be satisfied about the level of these resources. He added that there is a correlation between fees and the condition of the entity's financial reporting system: if the internal control does not operate properly and there are lots of mistakes, a high level of audit fees will be appropriate. However, if the level of fees is too low for a bank, that would be a concern. • Mr. Yurdakul concurred. 	<p>Support noted.</p> <p>See changes to the Task Force's approach to level of fees as noted above.</p>

Matters Raised	Task Force/ IESBA Response
<ul style="list-style-type: none"> Ms. McGeachy-Colby queried the rationale behind having a duplication of the requirement in the ISAs relating to the engagement partner in the Code. 	<p>Point taken into account.</p> <p>Mr. McPhee responded that national standard setters do not all implement the changes to the Code and auditing standards at the same time. In addition, the Task Force saw the benefit in having this requirement in the Code since this would be reinforcing the engagement partner's responsibility.</p> <p>Subsequently, the Task Force proposed that application material include reference to the auditing standards and the responsibility of the engagement partner for assigning or making available sufficient and appropriate resources to perform the audit.</p> <p>See proposed <i>paragraph 410.4 A1</i> in Agenda Item F1</p>
<ul style="list-style-type: none"> Ms. Pettersson noted the PIOB's support for the project. She highlighted that the business model of firms is changing as they are making investments in technology and developing new tools that could have an effect on the level of fees. In addition, new ways of service delivery could affect the fee charging models of the firms. She noted that this is a complex issue that would require the Task Force to engage in coordination with other Task Forces. 	<p>Points taken into account.</p> <p>See changes to the Task Force's approach to level of fees as noted above.</p> <p>The Task Force has also been coordinating its work with the NAS Task Force.</p>
PUBLIC DISCLOSURE OF LEVEL OF AUDIT FEES	
<ul style="list-style-type: none"> Mr. Hansen noted fees are very important from an ethical perspective. He was of the view that SMPs will push back on the proposal on public disclosure because that could raise issues of confidentiality. He also questioned the extent to which private entities can be compelled to disclose the fees they are paying to their auditors. He added that there might be unintended consequences, since firms could find ways to manipulate the presentation of fees in a disclosure. 	<p>Points accepted.</p> <p>The Task Force proposes a requirement for firms to ensure that the following fee-related information, is disclosed but only for PIEs:</p> <ol style="list-style-type: none"> Amount of fees paid for audit of financial statements Amount of fees paid to the audit client, other than as disclosed under point 1 Facts of fee dependency on the client. <p>In the case of items 1-2 above, this is usually made public by the client where required by law or</p>

Matters Raised	Task Force/ IESBA Response
<ul style="list-style-type: none"> Ms. McGeachy-Colby agreed with Mr. Hansen that such disclosure could raise concerns about confidentiality in the case of SMEs and SMPs. 	<p>regulation. In the case of information in point 3, the Code wouldn't require disclosing the specific ratio of total fees from the client, only the fact that fees from the client exceeded the ratio set out in the Code (15 percent).</p> <p>See proposed paragraph <i>R410.27</i> in Agenda Item F1.</p>
<ul style="list-style-type: none"> Mr. van der Ende was not supportive with the proposal regarding public disclosure since for regulators it is more important that the job is done properly. He added that disclosure is of lesser importance, especially in case of small banks. 	<p>Point taken into account.</p> <p>The Task Force considers that transparency of fee-related information, including public disclosure, is an effective tool in promoting independence in appearance.</p> <p>See <i>paragraph 410.22 A1</i> that includes the rationale for enhanced transparency in Agenda Item F1.</p>
<ul style="list-style-type: none"> Mr. Yurdakul noted that in some jurisdictions, regulators determine whether fee-related information should be made public or not. Accordingly, he cautioned that the proposed public disclosure by firms could create a conflict with national laws and regulations. He suggested reconsideration of the proposal and that public disclosure only be addressed if national laws and regulations do not address it. Mr. Thompson agreed, noting that in the UK, auditors have disclosed fees for a long time for both PIEs and non-PIEs. 	<p>Points accepted.</p> <p>During the meeting, Mr. McPhee responded that the Task Force is respectful of the role of regulators, but the Task Force found it important to have such a requirement at a global level, especially for jurisdictions where disclosure is not required by law or regulation.</p> <p>The Task Force does not intend to duplicate firms' obligation regarding public disclosure but build on the current laws and regulation. The Task Force proposes guidance on how to reconcile information required to be disclosed by existing laws and regulation and by the proposed provisions of the Code.</p> <p>See proposed <i>paragraph R410.27</i> in Agenda Item F1.</p>
<ul style="list-style-type: none"> Mr. Koktvedgaard asked for clarification about the geography of the disclosure, and wondered whether it would be in the audit report or the financial statements. If the former, he noted that there would be a need for coordination with the IAASB. 	<p>Based on the Task Force's proposals, firms would be required to be satisfied that certain fee-related information is publicly disclosed. Information can be published by the client or, if not possible, by the firm. The Code would provide guidance and examples as to the location of the disclosure. That would include, among others, the audit report as</p>

Matters Raised	Task Force/ IESBA Response
	<p>a suitable platform for such disclosure, with a reference to the relevant auditing standards.</p> <p>See proposed paragraphs <i>410.27 A3</i> and <i>410. A4</i> in Agenda Item F1.</p> <p>Point accepted regarding coordination with IAASB. See paragraphs 9-12 below in this document.</p>
FEE DEPENDENCY	
<ul style="list-style-type: none"> • Regarding the Task Force’s proposals for clients that are PIEs, Mr. Koktvedgaard suggested that the Task Force should be careful about potential unintended consequences for entry by new firms to the PIE audit market. • Mr. van der Ende agreed, adding that the Task Force’s proposals could affect second tier firms entering the PIE audit market. • Ms. Robert had the same view that the bar in the proposals may be too high. She mentioned, for example, that in the EU the threshold is at 3 consecutive years and there is no public disclosure but discussion with TCWG. • Dr. Lawal concurred with Ms. Robert. • Mr. Thompson agreed that more entrants are needed into the PIE audit market but there is also a need to make sure that firms have the resources to undertake the audits, especially for significant PIEs. 	<p>Points taken into account.</p> <p>During the meeting, Mr. McPhee responded that the Task Force would reflect further on the comments but that the Task Force did not intend to restrict new entrants to the PIE audit market.</p> <p>Subsequently the Task Force has revised its approach regarding the actions required after the first year of fee dependency.</p> <p>For PIE audit clients, the Task Force does not propose substantive changes regarding the actions that are required in the case of fee dependency. After two consecutive years, firm should whether determine pre-issuance review is an appropriate safeguard, as it is set out in the Extant Code as well, and public disclosure would be required also after the second year.</p> <p>However, in order to better inform the views and decisions of those charged with governance (TCWG) on fee-related matters, firms should disclose the fact of the fee-dependency to TCWG even after the first year.</p> <p>See proposed paragraphs <i>R410.16</i>, <i>R410.26</i> and <i>410.27 (c)</i> in Agenda Item F1.</p>
<ul style="list-style-type: none"> • Regarding the proposals for non-PIE audit clients, Mr. Fortin expressed support for the inclusion of a threshold for non-PIEs. 	<p>Support noted.</p>
<ul style="list-style-type: none"> • Concerning the safeguards applicable in case of fee dependency for non-PIE audit clients, Mr. Fortin asked whether the disclosure and 	<p>Point taken into account.</p> <p>The Task Force has revised its proposals in terms of safeguards for non-PIE audit clients, requiring</p>

Matters Raised	Task Force/ IESBA Response
<p>discussion with TCWG are appropriate safeguards. He wondered whether there should be an external party to undertake the review as he did not feel it would be credible to have someone internal to the firm to undertake it.</p> <ul style="list-style-type: none"> Mr. Koktvedgaard recommended the Task Force consider reporting to the regulator as a safeguard. 	<p>no communication with TCWG, but the review of the audit work after the audit opinion has been issued after 5 consecutive years of fee dependency. This review should be performed by a professional accountant outside of the firm, or by a professional body.</p> <p>See proposed paragraph <i>R410.13 (a)-(b)</i> in Agenda Item F1.</p>
<ul style="list-style-type: none"> Mr. van der Ende remarked that he did not see the rationale behind the Task Force’s proposals to address fee dependency and the role of transparency. He also provided examples when disclosure had unintended consequences (e.g. on salaries). 	<p>Point noted.</p> <p>The Task Force proposes general provisions and application material that includes the rationale and the role of transparency in mitigating threats.</p> <p>See proposed paragraphs <i>410.2</i> and <i>410.22 A1</i> in Agenda Item F1.</p>

Key Amendments to Task Force’s Proposals

Strengthening/Clarifying Link to Independence

- Fees or other types of remuneration derived from a client are commonly a significant driver of behavior. In the context of an audit engagement, fees can influence independence of mind and the level of these fees can also adversely impact perceptions of independence from the perspective of a reasonable and informed third party. Therefore, the Task Force proposes that the Code should include a general provision stating the fact that any type of fees paid to the firm by the audit client creates threats to independence. However, because of requirements for a firm to be independent when performing audit engagements and have in place a system of quality management that is designed (among other matters) to provide it with reasonable assurance in relation to compliance with independence requirements, the Task Force proposes that the Code recognize that the threats created by fees paid to an audit client will often be at an acceptable level.
- Nevertheless, to ensure that the threats to independence are at an acceptable level in the case of audit fees, the Task Force proposes that there be a requirement for a firm to be satisfied prior to the signing of the audit report that the level of the audit fee did not compromise the firm’s independence, and hence its ability to perform the audit in compliance with the fundamental principles, including in accordance with professional standards.
- In the case of specific types of fees (e.g. provision of services other than audit to the audit client) or fee-related circumstances (e.g. overdue fees or fee dependency), Section 410 sets out specific factors and safeguards to evaluate and address threats.
- In the case of audit clients that are public interest entities (PIEs), fees paid to a firm might result in a higher level of threat. Given the large number and wide range of stakeholders for PIEs, the Task Force proposes provisions to enhance the transparency of fee-related information of PIEs to assist in promoting independence, particularly in appearance.

Audit Fee as a Standalone Fee

- If a firm agrees to provide audit services at a lower fee because the audit client engages or promises to engage the firm or another a network firm for the supply of services other than audit (“low balling” audit fees), this creates an intimidation threat and might create a self-interest threat. The Task Force considers that the Code should include provisions concerning the special position of the audit fee, as a standalone fee, in the overall spectrum of fees received from the client. Therefore, the Task Force proposes a requirement that firms shall be satisfied that the provision of services other than audit to an audit client did not influence the level of the audit fee.
- In line with the principle recognized by the Code that determining fees is a business decision, firms are still able to decide on the overall amount of the fees, but any cost synergies should be reflected at the level of fees for services other than audit.

Proportion of Fees for Services Other than Audit to Audit Fee

- The Task Force proposes that the Code include provisions in circumstances where a large proportion of fees charged by the firm or a network firm to an audit client is generated by providing services other than audit. Responsive to Board members’ comments from the June IESBA meeting regarding

the difficulties in calculating the exact ratio of the fees, especially in the case of fees from network firms, the Task Force does not suggest adding any specific threshold to the Code. Firms can determine what would constitute a high proportion. However, factors are provided to assist in the evaluation of the level of the threats in this situation, which would then enable the firm to determine the appropriate actions to address the threats.

- In the case of PIE audit clients, the Task Force's current proposals rely more on transparency of information about fees paid for services other than audit by the audit client, and possible threats created by a high proportion of such fees to audit fees.

Streamlining Requirements Regarding Fee Dependency

- As the Board requested in June, the Task Force has streamlined the requirements and application material regarding fee dependency (when total fees generated from an audit client represent a large proportion of the firm's total fees). In doing so, the Task Force has endeavored to articulate the provisions in a way that preserves the key principle but allows sufficient flexibility.
- Aside from the provisions on factors and safeguards relevant to all audit clients, the Task Force proposes to retain the existing 15 percent threshold for PIE audit clients currently referenced in the Code. However, the Task Force proposes another threshold (30 percent) in case of non-PIEs. Firms would still be required to consider the relevant factors in evaluating the threats created by fee-dependency and apply appropriate safeguards to address the threats. However, once the relevant threshold is exceeded, the Code would require specific actions to be taken by firms, allowing greater latitude in the case of non-PIE audit clients.
- The Task Force also proposes that the Code articulate, as a key principle, that fee dependency on an audit client that is a PIE cannot continue for a prolonged period of time since a point will be reached at which threats can no longer be reduced to an acceptable level. In this context, the Task Force proposes that generally after a period of fee dependency for 5 consecutive years, the firm should cease to be the auditor. However, the Task Force recognizes circumstances raised by some Board members where it would be in the public interest for the firm to continue as auditor beyond such a period of 5 years. The Code would allow firms to continue the engagement for more than 5 years if there is a compelling public interest reason to do so and the firm has consulted with and received the concurrence of the relevant professional body.

Enhanced Transparency

- As the level of threats to independence, particularly independence in appearance, is greater for public interest entities, the Task Force believes that transparency regarding fee-related information, in terms of disclosure to those charged with governance and to the public, would be an effective measure to mitigate those threats. This recognizes that transparency has been an important factor in building trust and demonstrating independence within the body of professional standards.
- To provide a more cohesive approach to the Code's presentation of enhanced transparency of fee-related matters, the Task Force proposes a reordering of Section 410 and creating a separate subheading, "*Transparency of Information Regarding Fees for Audit Clients that are Public Interest Entities.*" The Code would articulate the rationale that transparency aims to provide information about fees to TCWG and to the public to better position them to form their views on the firm's independence and, in certain cases, make decisions related to appointment/reappointment of the auditors and on audit fees.

- Regarding communication with TCWG, the main purpose of the Task Force's proposals is to provide the basis for a meaningful discussion with TCWG about fee-related information, in line with requirements of ISA 260 on communication of independence matters.
- The proposed amendments concerning public disclosure set out a more flexible approach, focusing on guidance on how to achieve transparency for the benefit of the public. The Task Force proposes a few examples of possible locations for the disclosure, including the audit report, in circumstances where the information is not otherwise published by the audit client.

Revisiting Safeguards and Factors

- In line with the Project Proposal, the Task Force has revisited the safeguards and factors regarding evaluation of threats in relation to fees in the extant Code and is proposing revisions to align them to current best practice approaches.