

Fees – Proposed Revisions to Section 410

(Mark-up from Extant)

PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

SECTION 410

FEES

Introduction

- 410.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 410.2 In addition to a possible self-interest threat to compliance with one or more of the fundamental principles as set out in Section 330, fees or other types of remuneration paid to a firm might create a self-interest or intimidation threat to independence. ~~The nature and level of fees or other types of remuneration might create a self-interest or intimidation threat.~~ This section sets out specific requirements and application material relevant to applying the conceptual framework relating to fees charged to audit clients in such circumstances.

Requirements and Application Material

General

- 410.3 A1 The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements prepared by the audit client. This requires the auditor to be independent from the client. Where, as is generally the case, fees are also negotiated with and paid by the client, this creates a self-interest threat and might create an intimidation threat to independence.
- 410.3 A2 When the audit client is a public interest entity, stakeholders have heightened expectations regarding the firm's independence. As transparency can serve to better inform the views and decisions of those charged with governance and a wide range of stakeholders, this section provides for disclosure of fee-related information to both those charged with governance and stakeholders more generally for audit clients that are public interest entities.
- 410.3 A3 For the purposes of this section, audit fees comprise fees or other types of remuneration for an audit or review of financial statements. Where reference is made to the fee for the audit of the financial statements, this does not include any fee for an audit of special purpose financial statements or a review of financial statements.

Evaluating Threats

- R410.4 Before a firm accepts an audit or other engagement for an audit client, the firm shall determine whether the threats to independence created by the fees proposed to the client are at an acceptable level. The firm shall also make such determination where appropriate during the period of the audit engagement if circumstances change.
- 410.4 A1 Factors that are relevant in evaluating the level of threats created when fees for an audit or other engagement are paid by the audit client include:
- Whether there is external review of the quality of the firm's audit work.
 - The level of the fees and the extent to which they have regard to the resources required, taking into account the firm's commercial and market priorities and position.

- The involvement of those charged with governance in appointing the auditor and agreeing fees, and the apparent emphasis they and client management place on the quality of the audit and the level of the fees.
- Any linkage between fees for the audit and those for services other than audit, and the relative size of both elements.
- The extent of any dependency between the level of the fee for, and the outcome of, the service.
- The significance of the client to the firm.
- The nature of the client, for example whether the client is a public interest entity.

410.4 A2 The consideration of the factors in paragraphs 120.12 A3 (particularly the existence of a quality management system designed and implemented by the firm in accordance with [proposed] ISQM 1) and 410.4 A1 in the evaluation of the threats might often lead the firm to conclude that the threats are at an acceptable level.

410.4 A3 The requirements and application material that follow address circumstances where some of the factors in paragraph 410.4 A1 need further consideration in evaluating whether the threats are at an acceptable level. For those circumstances, there are examples of additional factors that are relevant in evaluating the threats.

Level of Audit Fees

410.5 A1 Determining the level of fees to be charged to an audit client, whether for audit or other services, is a business decision of the firm taking into account the facts and circumstances relevant to that specific engagement, including the requirements of technical and professional standards.

410.5 A2 In addition to the factors identified in paragraph 410.4 A1, factors that are relevant in evaluating the level of the threats created by the level of the audit fee when paid by the audit client include:

- The firm's commercial rationale for the audit fee.
- Whether there is a pressure applied by the client to reduce the audit fee.

410.5 A3 An example of an action that might be a safeguard to address such threats is having an appropriate reviewer who was not involved in the audit engagement review the work.

Impact of Other Services Provided to an Audit Client

410.6 A1 If a firm lowers the audit fee in the expectation that the audit client might engage the firm or a network firm for the provision of services other than audit, this increases the level of the self-interest threat and might also create an intimidation threat.

R410.7 A firm shall be satisfied that the provision by the firm or a network firm of services other than audit to an audit client does not influence the level of the audit fee.

410.7 A1 The level of the audit fee ordinarily reflects a combination of factors, such as those identified in paragraph 410.22 A1. However, the provision of other services to the audit client is not an appropriate factor in determining the level of the audit fee.

410.7 A2 Paragraph R410.7 is not intended to prohibit proper cost savings that can be achieved as a result of providing services other than audit to the audit client.

Contingent Fees

410.8 A1 Contingent fees are fees calculated on a predetermined basis relating to the outcome of a

transaction or the result of the services performed. A contingent fee charged through an intermediary is an example of an indirect contingent fee. In this section, a fee is not regarded as being contingent if established by a court or other public authority.

R410.9 A firm expressing the opinion on the financial statements of an audit client or a network firm participating in a significant part of the audit shall not charge directly or indirectly a contingent fee to the client unless for an audit engagement:-

- (a) It is for a non-assurance service provided to the client;
- (b) The fee receivable by the firm or the network firm is not material or expected to be material to such firm; and
- (c) The outcome of the non-assurance service, and therefore the fee, is not dependent on a future or contemporary judgement related to the audit of a matter that is material to the financial statements.

~~R410.11~~ A firm or network firm shall not charge directly or indirectly a contingent fee for a non-assurance service provided to an audit client, if:

- ~~(a) The fee is charged by the firm expressing the opinion on the financial statements and the fee is material or expected to be material to that firm;~~
- ~~(b) The fee is charged by a network firm that participates in a significant part of the audit and the fee is material or expected to be material to that firm; or~~
- ~~(c) The outcome of the non-assurance service, and therefore the amount of the fee, is dependent on a future or contemporary judgment related to the audit of a material amount in the financial statements.~~

410.9 A1 Paragraphs ~~R410.10 and R410.11~~ preclude a firm or a network firm from entering into certain contingent fee arrangements with an audit client. Even if a contingent fee arrangement is not precluded when providing a non-assurance service to an audit client, the level of the self-interest threat might still increase ~~be created~~.

410.9 A2 Factors that are relevant in evaluating the level of such a threat include:

- The range of possible fee amounts.
- Whether an appropriate authority determines the outcome on which the contingent fee depends.
- Disclosure to intended users of the work performed by the firm and the basis of remuneration.
- The nature of the service.
- The effect of the event or transaction on the financial statements.

410.9 A3 Examples of actions that might be safeguards to address such a ~~self-interest~~ threat include:

- Having an appropriate reviewer who was not involved in performing the non-assurance service review the work performed by the firm.
- Obtaining an advance written agreement with the client on the basis of remuneration.

Total Fees – Proportion of Fees for Services Other than Audit to Audit Fee

410.10 A1 When a large proportion of fees charged by the firm or network firms to an audit client is generated by providing services other than audit to the client, the level of the self-interest threat might increase or an intimidation threat might be created. This is due to concerns about the potential

loss of either the audit engagement or other services. A further consideration is a perception that the firm or network firm focuses on the non-audit relationship, which might create a threat to the auditor's objectivity.

410.10 A2 Factors that are relevant in evaluating the level of such threats include:

- The ratio of fees for services other than audit to the audit fee.
- The relationship to the audit client of the related entities for which the services other than audit are provided.
- The nature, scope and purposes of the services, including whether they are recurring services.
- The qualitative and quantitative significance of the client to the firm and to the network.
- The operating structure and the compensation arrangements of the firm and the network.

410.10 A3 An example of an action that might be a safeguard to address such self-interest or intimidation threats is having an appropriate reviewer who was not involved in the audit or the service other than audit review the relevant audit work.

Total Fees – Overdue

410.11 A1 The level of the self-interest threat might increase if fees payable by the audit client for the audit or services other than audit are overdue during the period of the audit engagement. ~~A self-interest threat might be created if a significant part of fees is not paid before the audit report for the following year is issued.~~ It is generally expected that the firm will require payment of such fees before such audit report is issued. The requirements and application material set out in Section 511 with respect to loans and guarantees might also apply to situations where such unpaid fees exist.

410.11 A2 Factors that are relevant in evaluating the level of such a self-interest threat include:

- The significance of the overdue fees to the firm.
- The firm's assessment of the ability and willingness of the client to settle the overdue fees.

410.11 A3 Examples of actions that might be safeguards to address such a self-interest threat include:

- Obtaining partial payment of overdue fees.
- Having an appropriate reviewer who ~~was not involved did not take part~~ in the audit engagement review the audit work performed.

R410.12 When a significant part of fees due from an audit client remains unpaid for a long time, the firm shall determine:

- (a) Whether the overdue fees might be equivalent to a loan to the client; and
- (b) Whether it is appropriate for the firm to be re-appointed or continue the audit engagement.

Total Fees – Fee Dependency~~Relative Size~~

All Audit Clients ~~All Audit Clients~~

410.13 A1 When the total fees generated from an audit client by the firm expressing the audit opinion represent a large proportion of the total fees of that firm, the dependence on ~~that client~~ and concern about the potential loss of fees from audit and other services from that client ~~losing the client~~ increase the level of the ~~create a~~ self-interest threat and create an ~~or~~ intimidation threat.

410.13 A2 In calculating the total fees of the firm, the firm might use financial information available from the previous financial year and estimate the proportion based on that information if appropriate.

410.13 A32 Factors that are relevant in evaluating the level of such threats include:

- The operating structure of the firm.
- ~~Whether the firm is well established or new.~~
- The qualitative and quantitative significance of the audit client ~~qualitatively and/or quantitatively~~ to the firm.
- Whether the firm is expected to expand such that the significance of the client is likely to reduce.

410.13 A43 ~~An~~ Examples of ~~an~~ actions that might be ~~a~~ safeguards to address such ~~a self-interest or intimidation~~ threats ~~include is~~

- Increasing the client base of in the firm to reduce dependence on the audit client.
- Increasing the extent of services provided to other clients.
- Reducing the extent of services other than audit provided to the client.
- Having an appropriate reviewer who was not involved in the audit engagement review the audit work.

410.13 A54 A self-interest or intimidation threats ~~are~~ also created when the fees generated by a firm from an audit client represent a large proportion of the revenue of one partner or one office of the firm.

410.13 A65 Factors that are relevant in evaluating the level of such threats include:

- The qualitative and quantitative significance of the audit client ~~qualitatively and/or quantitatively~~ to the partner or office.
- The extent to which the compensation of the partner, or the partners in the office, is dependent upon the fees generated from the client.

410.13 A76 Examples of actions that might be safeguards to address such self-interest ~~and/or~~ intimidation threats include:

- Increasing the client base of the partner or the office to reduce dependence on the audit client.
- Increasing the extent of services provided by the partner or the office to other clients.
- Reducing the extent of services other than audit provided by the partner or office to the client.
- Ensuring that the compensation of the partner is not significantly dependent on the fees generated from the client.
- Having an appropriate reviewer who was not involved ~~did not take part~~ in the audit engagement review the audit work.

Audit Clients that are Not Public Interest Entities

R410.14 When for each of five consecutive years total fees from an audit client that is not a public interest entity represent, or are likely to represent, more than 30% of the total fees received by the firm, the firm shall determine whether either of the following actions might be a safeguard to address the threats created, and if so, apply it:

- (a) Prior to the audit opinion being issued on the fifth year's financial statements, have a professional accountant, who is not a member of the firm expressing the opinion on the financial statements review the fifth year's audit work; or
- (b) After the audit opinion on the fifth year's financial statements has been issued, and before the audit opinion being issued on the sixth year's financial statements, have a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, or a professional body review the fifth year's audit work.

R410.15 If the total fees described in paragraph R410.14 continue to exceed 30%, the firm shall each year determine whether either of the actions in paragraph R410.14 applied to the relevant year's engagement might be a safeguard to address the threats created by the total fees received by the firm from the client, and if so, apply it.

R410.16 When two or more firms are engaged to conduct an audit of the client's financial statements, the involvement of the other firm in the audit may be regarded each year as an action equivalent to that in paragraph R410.14 (a), if:

- (a) The circumstances addressed by paragraph R410.14 apply to only one of the firms expressing the audit opinion; and
- (b) Each firm performs sufficient work to take full individual responsibility for the audit opinion.

Audit Clients that are Public Interest Entities

R410.174 When for each of two consecutive years the total fees from an audit client that is a public interest entity and its related entities represent, or are likely to represent, more than 15% of the total fees received by the firm, the firm shall determine whether, prior to the audit opinion being issued on the second year's financial statements, an engagement quality review performed by a professional accountant who is not a member of the firm expressing the opinion on the financial statements ("pre-issuance review") is a safeguard to address the threat, and if so, apply it. ~~Where an audit client is a public interest entity and, for two consecutive years, the total fees from the client and its related entities represent more than 15% of the total fees received by the firm expressing the opinion on the financial statements of the client, the firm shall:~~

- (a) ~~Disclose to those charged with governance of the audit client the fact that the total of such fees represents more than 15% of the total fees received by the firm; and~~
- (b) ~~Discuss whether either of the following actions might be a safeguard to address the threat created by the total fees received by the firm from the client, and if so, apply it:~~
 - (i) ~~Prior to the audit opinion being issued on the second year's financial statements, a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, performs an engagement quality control review of that engagement; or a professional body performs a review of that engagement that is equivalent to an engagement quality control review ("a pre-issuance review"); or~~
 - (ii) ~~After the audit opinion on the second year's financial statements has been issued, and before the audit opinion being issued on the third year's financial statements, a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, or a professional body performs a review of the second year's audit that is equivalent to an engagement quality control review ("a post-issuance review").~~

R410.5 ~~When the total fees described in paragraph R410.4 significantly exceed 15%, the firm shall determine whether the level of the threat is such that a post-issuance review would not reduce the~~

~~threat to an acceptable level. If so, the firm shall have a pre-issuance review performed.~~

~~**R410.6** If the fees described in paragraph R410.4 continue to exceed 15%, the firm shall each year:~~

~~(a) Disclose to and discuss with those charged with governance the matters set out in paragraph R410.; and~~

~~(b) Comply with paragraphs R410.4() and R410.5.~~

~~**R410.18** When two or more firms are engaged to conduct an audit of the client's financial statements, the involvement of the other firm in the audit may be regarded each year as an action equivalent to that in paragraph R410.17, if:~~

~~(a) The circumstances addressed by paragraph R410.17 apply to only one of the firms expressing the audit opinion; and~~

~~(b) Each firm performs sufficient work to take full individual responsibility for the audit opinion.~~

~~**R410.19** Subject to paragraph R410.20, if the circumstances described in paragraph R410.17 continue for five consecutive years, the firm shall cease to be the auditor after the audit opinion for the fifth year is issued.~~

~~**R410.20** As an exception to paragraph R410.19, the firm may continue to be the auditor after five consecutive years if there is a compelling reason to do so having regard to the public interest, provided that:~~

~~(a) The firm consults with the professional body or an independent regulatory body in the relevant jurisdiction and it concurs that having the firm continue as the auditor would be in the public interest; and~~

~~(b) Before the audit opinion on the sixth and any subsequent year's financial statements is issued, the firm engages a professional accountant who is not a member of the firm expressing the opinion on the financial statements to perform a pre-issuance review.~~

~~410.20 A1 A factor which might give rise to a compelling reason is the lack of viable alternative firms to carry out the audit engagement, having regard to the nature and location of the client's business.~~

Transparency of Information Regarding Fees for Audit Clients that are Public Interest Entities

Communication About Fee-related Information with Those Charged with Governance

~~410.21 A1 Communication by the firm of fee-related information (for both audit and services other than audit) with those charged with governance assists them in their assessment of the firm's independence. Effective communication in this regard also allows for a two-way open exchange of views and information about, for example, the expectations that those charged with governance might have regarding the scope and extent of audit work and impact on the audit fee.~~

Audit Fees

~~**R410.22** The firm shall communicate in a timely manner with those charged with governance of an audit client that is a public interest entity:~~

~~(a) The level of the fee for the audit of the financial statements;~~

~~(b) Any fees for the audit of special purpose financial statements and review engagements; and~~

~~(c) Whether the threats created by the level of the audit fees are at an acceptable level and any actions the firm has taken or proposes to take to reduce such threats to an acceptable level.~~

410.22 A1 The objective of such communication is to provide appropriate background and context regarding the audit fee. Such communication might therefore include matters such as:

- Considerations affecting the level of the fee such as:
 - The scale, complexity and geographic spread of the audit client's operations.
 - The time spent or expected to be spent commensurate with the scope and complexity of the audit.
 - The cost of other resources utilized or expended in performing the audit.
 - The quality of record keeping and processes for financial statements preparation.
- In the case of a group audit, the major elements of the audit fee, including the level of the fee for the audit of the financial statements which is paid or payable to each of the firm, network firms, or other audit firms for undertaking the audit.
- Any adjustments to the fee quoted or charged during the period of the audit, and the reasons for any such adjustments.
- Any changes to laws and regulations and professional standards relevant to the audit that impacted the fees.

410.22 A2 The firm is encouraged to provide such information as soon as practicable, preferably as part of the planning stage of the audit, with any proposed adjustments communicated as they are determined.

Fees for Services Other than Audit

R410.23 The firm shall communicate in a timely manner with those charged with governance of an audit client that is a public interest entity:

- (a)** The fees charged during the period covered by the financial statements for the provision by the firm or a network firm of services other than audit to the audit client (which for this purpose shall include only related entities over which the audit client has direct or indirect control): and
- (b)** Where the firm has identified that there is an increase in the level of the self-interest threat or that there is an intimidation threat to independence created by the proportion of such fees relative to the audit fee:
 - (i)** Whether such threats are at an acceptable level; and
 - (ii)** If not, any actions that the firm has taken or proposes to take to reduce such threats to an acceptable level.

410.23 A1 The objective of such communication is to provide appropriate background and context regarding the fees for services other than audit. Such communication might therefore include matters such as:

- The amount of fees from services other than audit that are required by laws and regulations.
- The nature of other services provided and their associated fees.
- Information on the nature of the services provided under a general policy approved by those charged with governance and associated fees. (Ref.: Para [Reference to be added to the application material arising from the NAS project regarding the examples to the processes the firm and those charged with governance may develop to obtain concurrence for the provision of non-assurance services])

- The proportion of fees referred to in paragraph R410.23(a) to the audit fee charged by the firm or network firms.

Fee Dependency

R410.24 Where the total fees from an audit client that is a public interest entity and its related entities represent or are likely to represent more than 15% of the total fees received by the firm, the firm shall communicate with those charged with governance:

- (a) That fact and whether this situation is likely to continue;
- (b) The safeguards applied to address the threats created, including, where relevant, the use of a pre-issuance review (Ref: Para R410.17); and
- (c) Any proposal to continue as the auditor under paragraph R410.20.

Public Disclosure of Fee-related Information

R410.25 The firm shall be satisfied that the following information is publicly disclosed in a timely and accessible manner:

- (a) Subject to paragraph R410.26, the level of the fee for the audit of the financial statements;
- (b) The amount of fees charged during the period covered by the financial statements for the provision by the firm or a network firm of services to the audit client (which, for this purpose shall include only related entities over which the client has direct or indirect control) other than as disclosed under (a); and
- (c) If applicable, the fact that the total fees received by the firm from the audit client and its related entities represent, or are likely to represent, more than 15% of the total fees received by the firm for two consecutive years, and the year that this situation first arose.

The requirements in subparagraphs (a) to (c) above may be met by compliance with laws and regulations which substantively satisfy the corresponding requirements.

410.25 A1 The fees disclosed usually reflect the fees paid or estimated to be paid for the services based on the information available at the time of the disclosure. The fees paid or estimated to be paid for the audit engagement include all such fees paid or payable to firms in relation to the audit work performed on which the audit opinion is based. In the case of a group audit, this would include the actual or estimated cost of work carried out by any component auditor at the request of the group engagement partner as set out in ISA 600.

410.25 A2 Examples of circumstances when compliance with laws and regulations would not substantively satisfy paragraph R410.25 include:

- In the case of a group audit, excluding fees charged by any component auditors carrying out work at the request of the group engagement partner.
- In the case of disclosure of fees for services other than audit, excluding fees for services provided by network firms to the audit client and related entities over which the client has direct or indirect control.

410.25 A3 In some circumstances, the audit client might agree to disclose such information, for example in its financial statements or annual report. Otherwise, the firm might consider other suitable locations, such as the proxy statement or the audit report for such disclosure.

410.25 A4 If the firm discloses the information required by paragraph R410.25 in the audit report, it would be appropriate to do so as part of the auditor's other reporting responsibilities in accordance with ISA 700 (Revised).

410.25 A5 The firm might also discuss with the client if disclosure of other information relating to fees might enhance the users' understanding. This might include matters such as:

- Comparative information for the prior year's fees for audit and services other than audit.
- In the case of a group audit, the major elements of the audit fee, including the level of the fee for the audit of the financial statements which is paid or payable to each of the firm, network firms, or other audit firms for undertaking the audit.
- The nature of services provided other than audit and their associated fees.
- Safeguards applied when the total fees from the client represent or are likely to represent 15% of the total fees received by the firm.

410.25 A6 The disclosure is regarded as accessible if the information required by paragraph R410.25 is readily available for any stakeholder in a manner that stakeholders are specifically informed about or the firm has reason to believe that stakeholders know about.

R410.26 Where the audit client does not make the disclosures specified in R410.25 and the firm is not able to obtain all the relevant information concerning the fee for the audit of the financial statements from a component auditor referred to in paragraph 410.25 A1, the firm shall be satisfied that that fact and the related circumstances have been disclosed.

Considerations for Review Clients

R410.27 This section sets out requirements for firms to communicate fee-related information of an audit client that is a public interest entity and be satisfied that such information is publicly disclosed. As an exception to those requirements, in the circumstance where a review client is not also an audit client, the firm may determine not to communicate or pursue disclosure of such information.