

## Fees – Proposed Revisions to the Code Arising from the Fees Project (Mark-up from Extant<sup>1</sup>)

### I. Proposals Arising from the Fees Project

The Task Force's proposals impact several sections of the Code and are set out in this document as follows:

- Section A, Proposed Revisions to Section 410, *Fees*
- Section B, Proposed Revisions to Section 270, *Pressure to Breach the Fundamental Principles*
- Section C, Proposed Consequential Amendments<sup>2</sup> to:
  - Section 330, *Fees and Other Types of Remuneration*;
  - Section 320, *Professional Appointment*; and
  - Section 400, *Applying the Conceptual Framework to Independence for Audit and Review Engagements*

### II. Proposals Arising from the Non-Assurance Services (NAS) Project

As noted in **Agenda Item 6**, the Task Force is coordinating with the NAS Task Force to develop some of its proposals (see paragraphs 410.15 A1 to 410.19 A1).

This notes in the gray boxes document explain the rationale for the significant revisions being proposed.

## Section A – Proposed Revisions to Section 410

### 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 The nature and level of fees or other types of remuneration derived from an audit client might create a self-interest or intimidation threat to independence. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

#### Requirements and Application Material

##### General

410.3 A1 Determining fees for an audit client, whether for audit or other services, is a business decision of the firm taking into account all the facts and circumstances relevant to that specific engagement, including the requirements of the professional standards. In this context, this section establishes requirements and application material for firms to address in considering facts and circumstances

<sup>1</sup> The extant Code is the 2018 versions of the Code which is revised and restructured. It will come into effect in June 2019.

<sup>2</sup> The Task Force anticipates that further conforming amendments will be needed to material in Part 4B of the Code.

that could influence the level of fees quoted or charged to an audit client, and which might create threats to independence.

**1. Note to paragraph 410.3 A1 and to explain the reordering of the material in Section 410**

*Location of Enhanced Provisions Related to Audit Fees*

- Section 330 of the Code, which addresses ‘Fees and Other Types of Remuneration’, explains that the level of fees quoted for professional services might create threats to compliance with fundamental principles, particularly with self-interest threat and compliance with professional competence and due care. However, certain circumstances could influence a firm’s decision in setting the level of audit fees and might also create threats to the firm’s independence. The Task Force believes that it is important to emphasize the likelihood that the level of fees quoted or charged might create threats to independence.
- Overall, it is important to emphasize that the proposed changes to the Code do not aim to affect the business decision of firms related to the fees quoted or charged for services provided to a client, however the Task Force’s proposals do require that irrespective of the fees quoted or charged, the firm’s ability to perform the audit in accordance with professional standards shall not be affected. Further, recognizing that transparency has been an important factor in building trust and demonstrating independence within the body of professional standards, the Task Force has considered the opportunities for enhancing transparency in respect of fee-related matters in both communication with those charged with governance, and more broadly with external stakeholders, where this would be beneficial (namely for certain disclosures for audit clients that are public interest entities).

**Nature and Level of Audit Fees**

*All Audit Clients*

410.4 A1 In this section, audit fees consist of all types and nature of payments quoted or charged by the firm for performing the audit engagement, including any adjustments and variations to amounts originally proposed.

Level of Audit Fees

R410.5 A firm shall be satisfied prior to the signing the audit report that the audit fees did not affect the firm’s ability to perform the audit in accordance with professional standards.

410.5 A1 The IAASB’s International Standards establish the responsibilities for the firm, network firm and the engagement partner with respect to the audit. With respect to the audit engagement, the engagement partner is responsible for ensuring that there are sufficient and appropriate resources assigned or made available to perform the audit engagement, irrespective of the fees quoted or charged.

Other Services Provided to an Audit Client

R410.6 The firm shall be satisfied that the provision, or possible provision, of services other than audit to an audit client does not influence the level of audit fees.

410.6 A1 The level of audit fees ordinarily reflects the skills and experience of the personnel and the time spent and the cost of other resources expended in performing the audit and the competitive position in the market place. The audit fee should be determined on the assumption that no other services are provided to the audit client. This is not intended to prevent a firm recognizing that there may be appropriate cost synergies should such services other than audit be provided, but should such synergies arise they should be reflected in the fees for the services other than audit.

## Contingent Audit Fees

**R410.10R410.7** A firm shall not quote or charge directly or indirectly a contingent fee for an audit engagement.

**410.9 A1410.7 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 quoted or 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.

### **2. Note to paragraph 410.4 A1**

#### *Definition of Audit Fees*

- As part of the new subsection on Nature and Level of Audit Fees, the Task Force proposes that the Code include an explanation (or definition) of audit fees. This will allow for better understanding and application of the provisions in Section 410 because it will focus on the type and nature of payments quoted or charged by the firm in exchange for an audit. In other words, audit fees should encompass any kind of payment quoted or charged by the firm during the audit, including adjustment or variations made after the acceptance of the engagement.
- Since this definition is not relevant for other section of the Code, based on the Drafting Guidelines, the Task Force proposes including the description of audit fees as application material in Section 410 and not as part of the Glossary.

### **3. Note to paragraphs R410.5 and 410.5 A1**

#### *Level of Audit Fees (Including Responsibility of Firm and Engagement Partner)*

- As reflected in para R410.5, irrespective of the facts and circumstances that determine the level of audit fees, the Task Force proposes that the fee quoted or charged should allow the firm to perform the audit in accordance with professional standards. This overarching principle to be applied when determining the level of audit fees is in line with the new ISQM 1 and ISA 220. Therefore, the Task Force recommends the Code include a reference, as application material, to the relevant provisions in the ISAs.

### **4. Note to paragraphs R410.6 and R410.6 A1**

#### *Undue Influence of Other Services to Audit Fees*

- When entering into discussions or negotiations on audit fees and total fees for providing certain services to an audit client, there are many factors that could influence the total fees charged for that particular client. The quantum of these fees is a business decision. A firm can quote or charge whatever fee is considered appropriate.
- However, to complement the March 2019 proposal that audits are to be performed in accordance with professional standards, the Task Force also proposes a requirement that when a firm provides other services, the provision of those services shall not influence the level of audit fees quoted. In other words, fees for an audit engagement should stand alone, and should not be considered as part of a spectrum of total fees and provision of other services which could result in changes to the level of audit fees.

## Audit Clients that are Public Interest Entities

**410.8 A1** The level of audit fees for an audit client that is a public interest entity is relevant information for a large number of external stakeholders in considering the audit undertaken by a firm. The disclosure of the level of audit fees also reflects the profession's recognition of the professional accountant's public interest responsibility. Some jurisdictions might have existing provisions that are intended to enhance transparency about audit fees and other fee-related matters.

## Communication of Audit Fee-related Matters to Those Charged with Governance

**R410.9** The firm shall communicate in a timely manner the firm's compliance with paragraph R410.5 and other relevant information about the audit fees, including the level of fees, to those charged with governance of an audit client that is a public interest entity.

**410.9 A1** Examples of relevant information about the audit fees include:

- Considerations affecting the resources allocated to the audit such as
  - the scale and complexity of operations,
  - geographic spread,
  - the need to utilize specialist resources, and
  - the quality of record keeping and processes for financial statements preparation.
- Any adjustments or variations to the fees quoted or charged during the course of the audit, and the reasons for any such adjustments.
- Basis for determining audit fees for components.
- Any changes to national laws and professional standards relevant to the audit undertaken.
- Timing of the work within the annual cycle and deadline provided for the issuance of the audit report, such as an accelerated reporting timeline or statutory filing timeline.

**410.9 A2** In order to allow those charged with governance to be given relevant information about the audit fees in a timely manner, the firm is encouraged to provide such information as soon as practicable. Preferably, this should occur as part of the planning stage of the audit with any proposed adjustments communicated as the firm determines them. If adjustments are determined after the issuance of the audit report, such adjustments also form part of the required communication.

**410.9 A3** The requirements and application material in paragraphs R300.10 to 300.10 A1 apply when determining the appropriate individuals within the entity to whom the firm communicates.

**410.9 A4** If the firm has not communicated its compliance as set out in R410.9 and concludes that a breach has occurred, the requirements and application material paragraphs R400.80 to R400.89 apply.

## Public Disclosure of Audit Fees

**R410.10** In a number of jurisdictions there are laws and regulations concerning the responsibility of the audit client and the firm with respect to the public disclosure of audit fees or transparency about fees paid to audit firms more broadly. In such circumstances the firm shall obtain an understanding of relevant laws and regulations and comply with them, where applicable.

**410.10 A1** Section 360 – *Responding to Non-Compliance with Laws and Regulations* sets out requirements and application material that is relevant when responding non-compliance or suspected non-compliance by the audit client with laws and regulations that relate to the disclosure of audit fees.

**R410.11** If not otherwise publicly available, the firm shall disclose the amount of audit fees for an audit client that is a public interest entity in the audit report, unless such disclosure is prohibited by laws or regulations.

**410.11 A1** The audit fees disclosed should reflect the fees paid or estimated to be paid for the audit engagement based on the information available at the time of the disclosure. Any subsequent adjustments made should be disclosed, if practicable, at the same time as that relating to the subsequent audit engagement. Circumstances under which such disclosure might not be practicable include a change of firm.

410.11 A2 The fees paid or estimated to be paid for the audit engagement include all such fees paid or payable to firms in relation to audit work performed on which the audit opinion is based. In the case of a group audit this would include the audit work carried out by a component auditor at the direction of the group audit engagement partner as set out in ISA 600, *Special Consideration- Audits of Group Financial Statements (Including the Work of Component Auditor)*.

410.11 A3 Other information that is relevant to the amount of the audit fees may be disclosed in the audit report to enhance the reader's understanding of the overall audit fee information. Examples of such information include:

- The fees paid or payable to (each of) the firm(s) providing the audit opinion.
- The fees paid or payable to other firms in the same network(s) as the firm(s) providing the audit opinion.
- The fees paid or payable to other firms that carried out work in relation to the audit engagement.
- Where the audit opinion covers the financial statements of both a single legal entity and its consolidated group, the split of the audit fees between those elements.

R410.12 The requirements and application material in paragraph R410.10 to 410.11 A3 relating to public disclosure of audit fees shall not apply to engagements for the audit of special purpose financial statements and to review engagements.

## **5. Note to paragraphs R410.9 to 410.9 A4**

### *Auditor Communication to Those Charged with Governance (TCWG)*

- ISA 260 (Revised) set out requirements for auditor communication with TCWG. These provisions apply to listed entities. However, the Task Force considers that the communication related to the level of fees should go beyond a factual statement about the level of audit and other fees and that the communication should apply to all public interest entities (PIE), and not only for listed entities.
- The Task Force's aim is to create a more meaningful basis for auditor communication with TCWG than is currently required, involving communication of relevant facts and circumstances related to fees that would allow TCWG to be better informed about the level of fees quoted or charged. This information would help TCWG assess whether auditors have performed the audit in accordance with professional standards.
- The Task Force considered that the engagement partner would be the best positioned to initiate such communication, however, having regard to overarching principles in Part 4A (see paragraph 400.4) on not establishing specific responsibility of individuals within the firm related to independence, the Task Force only refers to the firm in this provision for the ease of reference.

## **6. Note to paragraphs R410.10 to 410.12**

### *Public Disclosure*

- Based on the earlier fact-finding activities, the Task Force was aware that some jurisdictions have laws and regulations requiring public disclosure of fee-related information. Further, the Task Force recognizes that the primary source of this information should desirably be the client's financial statements. Nevertheless, recognizing the stakeholders' interests in having access to fee-related information, as a key element in forming an opinion on the firm's independence, the Task Force considers there is a strong case for firms to carry the responsibility of having such information properly disclosed where this information is not available from the client's financial statements.
- For these reasons, the Task Force's proposals takes into account current national rules and regulations

but also establishes a responsibility for firms to publicly disclose fee related information in circumstances when national laws and regulations do not address the public disclosure of fee related information.

- To provide the same level of accessibility to this information, the Task Force proposes the audit report, as a common platform, for the location of this disclosure, when required.
- As part of the disclosure, similarly to the disclosure to TCWG, the Task Force is of the view that for the disclosure of certain other information relevant to the amount of the audit fees would also be appropriate to contribute to the reader's overall understanding of the determination and structure of the audit fees.
- Regarding the amount of the fee to be disclosed, the Task Force proposes the application material in paragraphs 410.11 A1 and 410.11 A2, that would apply when national laws and regulations do not have specific provisions.

## **Nature and Level of Fees for Services Other than Audit from an Audit Client**

### **Contingent Fees for Services Other than Audit from an Audit Client**

#### **Non-Assurance Services Provided to an Audit Client**

**R410.13** A firm or network firm shall not quote or charge directly or indirectly a contingent fee for a non-assurance service provided to an audit client, if:

- (a) The fee is quoted or 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 quoted or 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.

**410.13 A1** Paragraphs R410.~~740~~ and R410.~~1344~~ preclude a firm or, as applicable, 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, a self-interest threat might still be created.

**410.13 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.

**410.13 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.

#### **Assurance Services Provided to an Audit Client**

**410.14 A1** Paragraphs 905.6 A1 to 905.9 A3 in Part 4B – *Independence for Assurance Engagements Other*

than Audit and Review Engagements set out requirements and application material for contingent fees for an assurance client that is also an audit client.

Communication with Those with Charged with Governance Relating to Fees for Services Other than Audit

All Audit Clients

410.15 A1 Paragraphs R300.9 to 300.9 A2, 400.40 A1 and 400.40 A2 set out requirements and application material that are relevant when communicating with those charged with governance, including information on fees for services other than audit from an audit client.

Audit Clients that are Public Interest Entities

**R410.16** A firm shall communicate to those charged with governance in a timely manner the fees quoted or charged for provision by the firm or network firm of services other than audit to an audited entity that is a public interest entity and to related entities over which the audited entity has direct or indirect control.

Ratio of Audit Fees and Fees for Services Other than Audit

All Audit Clients

410.17 A1 When a large proportion of fees charged to an audit client is generated by providing services other than audit to the audit client, the dependence on that client and the risk of losing the engagements, other than the audit, create a self-interest or intimidation threat.

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

- The nature, scope and purpose of the service.
- The significance of the client qualitatively and quantitatively to the firm.
- The operating structure of the firm.

410.17 A3 An example of action that might be safeguard to address such self-interest or intimidation threat is having an appropriate reviewer who did not take part in the audit engagement review the work.

Audit Clients that are Public Interest Entities

**R410.18** When a firm provides services other than audit to an audited entity that is a public interest entity, the firm shall communicate to those charged with governance the ratio of audit fees, and total fees for services other than audit charged during the period covered by the financial statements by the firm to the audited entity and the entities over which the audited entity has direct or indirect control.

**R410.19** If for three consecutive years the total fees for services other than audit charged by the firm to an audited entity that is a public interest entity and to entities over which the audited entity has direct or indirect control exceeds 70% of the average of the last three years' fees for the audit, the firm shall:

- (a)** Disclose to those charged with governance the fact that total fees for the services other than audit from an audited entity and entities over which the audited entity has direct or indirect control has exceeded 70% of the average of the last three years' fees received from that audited entity for audit;
- (b)** Discuss with those charged with governance whether prior to the audit opinion being issued on the third year's financial statements an engagement quality review of that engagement performed by a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, or a review of that engagement that is equivalent to an

engagement quality review performed by a professional body, (“a pre-issuance review”) might be a safeguard to address the threat and if so, apply it.

(c) Disclose publicly in the audit report the fact that total fees for the services other than audit from an audited entity and entities over which the audited entity has direct or indirect control has exceeded 70% of the average of the last three years’ fees received from that audited entity for audit.

410.19 A1 The firm might also disclose information in the audit report that is relevant to understanding the ratio described in paragraph R410.19. Examples include:

- The ratio of audit fees and total fees for services other than audit charged by the firm or network firm during the period covered by the financial statements.
- Whether services other than audit provided to an audit client are required by laws and regulations.

#### **7. Note to the above subsection on Nature and Level of Fees for Services Other than Audit**

- Similar to audit fees, the nature and level of fees charged or quoted for any services, other than audit, to the audit client could also compromise the independence of the firm, especially if the fees for those other services constitute a significant proportion of the total fees received from that audit client.
- The Task Force is of the view that firms should be required to evaluate, and address threat created not only by level of fees for non-assurance services, but all services other than audit (i.e. other assurance services) provided to an audit client. In the case of existing provisions related to fees for assurance services, such as contingent fees, the Task Force proposes that reference be made to relevant provisions of Part 4B of the Code, on *Independence for Assurance Engagements Other than Audit and Review Engagements*.
- For its proposals, the Task Force adopted the following as a basis:
  - the provisions of the current Code on fees for non-assurance services, and
  - proposals of the NAS Task Force on fees for non-assurance services.

#### **8. Note to paragraph R410.16**

##### *Communication with TCWG Relating to Fees for Services Other than Audit*

- ISA 260 (Revised) notes that auditor communication with TCWG on issues related to auditor’s independence “shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity”<sup>3</sup>. However, to provide better information for TCWG, the Task Force proposal is to require communicating the amount charged for a service other than audit on a case by case basis, in a timely manner.
- Following the concept reflected in the ISA 260 (Revised), the Task Force proposes that firms communicate to TCWG the information related to fees charged for the provision of services other than audit charged by the firm or the network. Nevertheless, in line with the wording of ISA 260 (Revised), and with regard to practicality, the firm should include, as part of the communication, only such fees that were charged for the audit client and for entities over which the audit client has direct or indirect control. Since by definition, reference to audit client that is a listed entity encompasses all related entities (see paragraph R400.20), the Task Force proposes using the term “audited entity” instead of “audit client” to avoid that contention.

<sup>3</sup> Paragraph 17 of ISA 260 (Revised)

## 9. Note to paragraphs 410.17 A1 to 410.19 A1

### *Ratio of Audit Fees and Fees for Services Other than Audit*

- The Task Force proposes the Code set out provisions related to threats created by having a large proportion of the fees generated from providing services other than audit to the audit client, such as factors and safeguards on how to evaluate and address those threats.
- In the case of audit clients that are public interest entities the Task Force is of the view that there would be benefit in providing information to TCWG on the ratio of the quantum of the fees.
- The Task Force considered requiring public disclosure on the quantum of the fees as well, however, after consulting with the NAS Task Force, concluded that the effect of the prohibition related to self-review threat will reduce the level of NAS fees, therefore the disclosure of fees for services other than audit might not be necessary.
- Following up the NAS Task Force previous proposal, in case of PIE audit clients, if that ratio exceeds a certain threshold, the Task Force proposes that firms be required to reassess the threats created. The Task Force's proposal does not intend to create a "fee cap" for services other than audit provided to an audit client, only requires certain actions (disclosure of this fact to TCWG and to the public) and application of safeguards to address the threat created by exceeding certain ratio of fees. The proposed threshold harmonizes with the Article 4 of the [EU Regulation](#).

## **Total Fees – Relative Size**

### **All Audit Clients**

410.~~203~~ 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 losing the client create a self-interest or intimidation threat.

410.~~203~~ A2 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 significance of the client qualitatively and/or quantitatively to the firm.

410.~~203~~ A3 An example of an action that might be a safeguard to address such a self-interest or intimidation threat is increasing the client base in the firm to reduce dependence on the audit client.

410.~~203~~ A4 A self-interest or intimidation threat is 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.~~203~~ A5 Factors that are relevant in evaluating the level of such threats include:

- The significance of the 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.~~203~~ A6 Examples of actions that might be safeguards to address such self-interest or intimidation threats include:

- Increasing the client base of the partner or the office to reduce dependence on the audit client.
- Having an appropriate reviewer who did not take part in the audit engagement review the work.

Audit Clients that are Not Public Interest Entities

**R410.21** When total fees from the 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 expressing the opinion on the financial statements of the client for five consecutive years, the firm shall determine 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:

**(a)** Prior to the audit opinion being issued on the fifth 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 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

**(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, 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 fifth year's audit that is equivalent to an engagement quality review ("a post-issuance review").

410.21 A1 In calculating the total fees to be received by the firm in this section, the firm might use financial information available from the previous financial year and estimate the proportion based on that information.

**R410.22** If the total fees described in paragraph R410.21 continue to exceed 30%, the firm shall each year determine whether either of the actions in paragraph R410.21 (a) or (b) applied to the relevant year's engagement 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.

**R410.23** In the case of a joint audit, where R410.21 applies to one of the firms expressing the audit opinion, then provided the total fees received by the other firm represents less than 30% of the total fees received by that other firm, then this may be regarded as providing a safeguard equivalent to that in R410.21 (a).

Audit Clients that are Public Interest Entities

Addressing Fee-dependency

**R410.24** Where an audit client is a public interest entity and the total fees from the client and its related entities are likely to 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 disclose to and discuss with those charged with governance of the audit client the fact that the total of such fees are likely to represent more than 15 % of the total fees received by the firm.

410.24 A1 In calculating the total fees to be received by the firm in this section, the firm might use financial information available from the previous financial year and estimate the proportion based on that information.

410.24 A2. Where an audit client is a public interest entity and the fees described in paragraph R410.24 exceed 15 %, and it is likely that will exceed 15 percent in the following year, it might be appropriate for the firm to disclose the current year position publicly in the audit report.

**R410.254** 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: Where an audit client is a public interest entity and the fees described in paragraph R410.24 continue to exceed 15 %, the firm shall each year:

- (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 with those charged with governance whether a pre-issuance review 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, and:
- (c) Disclose publicly in the audit report the fact that the total of such fees represents more than 15% of the total fees received by the firm.
- ~~(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").~~

#### Addressing High Levels of Fee Dependency

**R410.265** ~~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. When an audit client is a public interest entity and the total fees from the client and its related entities are likely to substantially exceed 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 are likely to substantially exceed 15% of the total fees received by the firm
- (b) Comply with paragraph R410.25 (b), and
- (c) Disclose publicly in the audit report the fact that the total of such fees represents substantially more than 15% of the total fees received by the firm.

**R410.27** ~~When determining whether the total fees received from an audit client that is a public interest entity substantially exceeds 15 %, the firm shall exercise professional judgment and take into account whether a reasonable and informed third party would likely to reach the same conclusion.~~

410.27 A1 Factors that are relevant in determining the significance of total fees from the audit client that is a public interest entity include:

- The fact that total fees from the client and its related entities represents more than 30 % of the total fees received by the firm.
- Any non-recurring, significant facts and circumstances that are likely to affect the performance and the complexity of the audit engagement, such as mergers and acquisitions at the audit client or at the firm.
- Changes affecting the client-base of the firm, such as laws and regulation requiring mandatory firm rotations.

**R410.286** ~~If an audit client is a public interest entity and the fees described in paragraph R410.426 continue to substantially exceed 15%, the firm shall each year, for the next four years, comply with R410.26:~~

~~(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.~~

**R410.29** In the case of a joint audit where R410.25 to R410.28 applies to one of the firms expressing the audit opinion, then provided the total fees received by the other firm represents less than 30% of the total fees received by that other firm, then this may be regarded as providing a safeguard equivalent to that in R410.25 (b).

**R410.30** If an audit client is a public interest entity and the fees described in paragraph R410.26 continue to substantially exceed 15 % for five consecutive years, the firm shall cease to be the auditor after the audit report for the fifth year is issued. Before resigning, the firm shall take into consideration, and take actions to comply with, laws and regulations governing auditor resignations.

## 10. Note to paragraphs R410.21 to R410.23

### *Fee-Dependency of non-PIEs*

- The Task Force has proposed a similar model for firms addressing the threats to the fundamental principles for non-PIE audit clients as for the Code's existing fee-dependency model for PIE audit clients, but allowing greater latitude in the thresholds and safeguards adopted.<sup>4</sup> The Task Force considered this would be a reasonable approach bearing in mind the nature of the threats, SMP considerations, the public interest, and the pending IESBA initiative on the definition of PIEs, defined in the [Strategy and Working Plan 2019-2023](#), that will be launched sooner, based on the Board's decisions in March 2019.
- In the case of non-PIE audit clients, the Task Force does not propose, on balance, communication with TCWG, given the governance arrangements commonly applying and relevant threats, but would require the firm to determine whether a post-issuance or pre-issuance review would be appropriate.
- The Code would also give guidance on the determination of total fees of the firm, suggesting using the information available from the previous financial year as one source of available information.
- In the case of a joint audit, as an exception, the Task Force proposes that the firm need not consider applying pre-issuance or post-issuance review, if one of the firms issuing the audit report does not have significant fee-dependency issues with the audit client.

## 11. Note to paragraphs R410.24 to R410.30

### *Fee-Dependency of PIEs*

- Taking into account the comments provided during the March 2019 Board meeting and the concerns raised by some jurisdictions, the Task Force has revised its initial proposals. The Task Force suggests that the Code set out different regimes for cases when the amount of fees from one PIE audit client exceeds 15 percent of the total fees, and for those cases when total fees 'substantially' exceed 15 percent. Paragraph 410.27 A1 includes guidance on how to determine if total fees substantially exceed 15 percent.
- To better differentiate between the two regimes, the Task Force recommends moving away from the term "significantly", that is currently used in the Code, and using a term that might better demonstrate the differential – which potentially can be double the 15% baseline amount when additional requirements

<sup>4</sup> The Task Force considered whether to include all related entities within the definition of non-PIE audit clients. However, concerns were raised that gathering relevant information in relation of fees, particularly in the case of sister entities, might be difficult. For that reason, the Task Force agreed to follow the approach taken previously by the IESBA and not to propose any changes to evaluation of related entities of non-PIE audit clients.

apply (e.g., communication with TCWG and public disclosure of the higher level of fee dependency).

- In addition, the Task Force is of the view that in cases where total fees from one PIE audit client substantially exceed 15 percent, different rules should apply even in the first year, and having regard to the public interest, a firm would be required to publicly disclose that information in the audit report.
- In cases where fees from one PIE audit client substantially exceed 15 percent of the total fees for 5 consecutive years, only if the percentage is substantial every year, the firm would be required to cease the engagement, taking into account consideration of any national laws and regulations governing auditor resignations. The Task Force is of the view that this requirement might also be a factor for firms to consider before planning on expanding the revenue from an already significant audit client.
- The table below summarizes the proposed provisions to PIE audit clients:

Total fees / years	In any given year	More than 1 year	More than 5 years
Exceed 15 %	<ul style="list-style-type: none"> <li>• Disclose and discuss with TCWG</li> <li>• [+ Public disclosure encouraged]</li> <li>• No additional safeguards required</li> </ul>	<ul style="list-style-type: none"> <li>• Disclose and discuss with TCWG</li> <li>• Pre-issuance review</li> <li>• Public disclosure</li> </ul>	-
Substantially exceed 15 %	<ul style="list-style-type: none"> <li>• Disclose and discuss with TCWG</li> <li>• Public disclosure</li> <li>• No additional safeguards required</li> </ul>	<ul style="list-style-type: none"> <li>• Disclose and discuss with TCWG</li> <li>• Pre-issuance review</li> <li>• Public disclosure</li> </ul>	Exit

### **Total Fees – Overdue Fees**

410.317 A1 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.

410.317 A2 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 did not take part in the audit engagement review the work performed.

**R410.328** 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.

**Contingent Fees** [The provisions relating to contingent fees have been moved up (see paragraphs R410.7 and R410.13 above)]

## Section B – Proposed Revisions to Section 270

### SECTION 270

#### PRESSURE TO BREACH THE FUNDAMENTAL PRINCIPLES

...

#### Requirements and Application Material

##### General

**R270.3** A professional accountant shall not:

- (a) Allow pressure from others to result in a breach of compliance with the fundamental principles; or
- (b) Place pressure on others that the accountant knows, or has reason to believe, would result in the other individuals breaching the fundamental principles.

270.3 A1 A professional accountant might face pressure that creates threats to compliance with the fundamental principles, for example an intimidation threat, when undertaking a professional activity. Pressure might be explicit or implicit and might come from:

- Within the employing organization, for example, from a colleague or superior.
- An external individual or organization such as a vendor, customer or lender.
- Internal or external targets and expectations.

270.3 A2 Examples of pressure from others that might result in threats to compliance with the fundamental principles include:

- Pressure related to conflicts of interest:
  - Pressure from a family member bidding to act as a vendor to the professional accountant's employing organization to select the family member over another prospective vendor.

See also Section 210, *Conflicts of Interest*.

- (...)

270.3 A3 An example of pressure placed on others that might result in threats to other individuals' compliance with the fundamental principles would be pressure exerted on another professional accountant to provide professional services at a fee level that did not allow for sufficient and appropriate resources to perform the services in accordance with professional standards.

270.3 A~~4~~<sup>3</sup> Factors that are relevant in evaluating the level of threats created by pressure include:

- The intent of the individual who is exerting the pressure and the nature and extent of the pressure.
- ....

## Section C – Proposed Revisions to Sections 330, 320 and 400

### SECTION 330

#### FEES AND OTHER TYPE OF REMUNERATION

...

#### Application Material

##### Level of Fees

- 330.3 A1 The level of fees quoted might impact a professional accountant's ability to perform professional services in accordance with professional standards.
- 330.3 A2 A professional accountant might quote whatever fee is considered appropriate. Quoting a fee lower than another accountant is not in itself unethical. However, the level of fees quoted creates a self-interest threat to compliance with the principle of professional competence and due care if the fee quoted is so low that it might be difficult to perform the engagement in accordance with applicable technical and professional standards.
- 330.3 A3 Factors that are relevant in evaluating the level of such a threat include:
- a) Whether the client is aware of the terms of the engagement and, in particular, the basis on which fees are charged and which professional services the quoted fee covers.
  - b) Whether the level of the fee is set by an independent third party such as a regulatory body.
- 330.3 A4 Examples of actions that might be safeguards to address such a self-interest threat include:
- c) Adjusting the level of fees or the scope of the engagement.
  - d) Having an appropriate reviewer review the work performed.
- 330.3 A5 Requirements and application material related to the level of fees for audit and review engagements are set out in the International Independence Standards.

### SECTION 320

#### PROFESSIONAL APPOINTMENT

...

#### Requirements and Application Material

##### Client and Engagement Acceptance

###### General

- 320.3 A1 Threats to compliance with the principles of integrity or professional behavior might be created, for example, from questionable issues associated with the client (its owners, management or activities). Issues that, if known, might create such a threat include client involvement in illegal activities, dishonesty, questionable financial reporting practices or other unethical behavior.
- 320.3 A2 ...
- 320.3 A3 A self-interest threat to compliance with the principle of professional competence and due care is created if the engagement team does not possess, or cannot acquire, the competencies to perform the professional services.
- 320.3 A4 Factors that are relevant in evaluating the level of such a threat include:
- An appropriate understanding of:
    - The nature of the client's business;

- The complexity of its operations;
- The requirements of the engagement; and
- The purpose, nature and scope of the work to be performed.
- Knowledge of relevant industries or subject matter.
- Experience with relevant regulatory or reporting requirements.
- The existence of quality control policies and procedures designed to provide reasonable assurance that engagements are accepted only when they can be performed competently.
- A level of fees that allows for sufficient and appropriate resources (including human, technological and intellectual property resources) to perform the engagement.

320.3 A5 Examples of actions that might be safeguards...

...

## **SECTION 400**

### **APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS**

#### **Introduction**

##### **General**

- 400.1 It is in the public interest and required by the Code that professional accountants in public practice be independent when performing audit or review engagements.
- 400.2 This Part applies to both audit and review engagements unless otherwise stated. The terms “audit,” “audit team,” “audit engagement,” “audit client,” and “audit report” apply equally to review, review team, review engagement, review client, and review engagement report.
- 400.3 In this Part ....

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