

Fees – Issues and Task Force Proposals

How the Project Serves the Public Interest

The fees project is responsive to a public interest need for the IESBA to deal with fee-related matters, including those that impact, or are perceived to impact auditor independence – both independence of mind and independence in appearance. In this context, the project responds to concerns raised by the Public Interest Oversight Board (PIOB) and the regulatory community, in particular, the International Organization of Securities Commissions (IOSCO).

Summary of Proposals to Strengthen the Fee-related Provisions in the Code

Level of Fees

Strengthening Provisions including Clarification of Responsibilities for Engagement Partners

- Establish a requirement for firms to be satisfied that the fees quoted for audit engagements do not affect the firm's¹ ability to perform the audit in accordance with professional standards.
- Establish a requirement for the engagement partner to determine whether sufficient and appropriate resources (including personnel, technological and intellectual property resources) are assigned or made available to perform the engagement, irrespective of the fees quoted.
- Enhance the current provisions related to the acceptance of a new engagement by adding the level of fees as a factor for firms to consider in assessing relevant threats.

New Application Material to Signal How Pressure Exerted by a PAIB Might Create a Threat

- Add new application material to signal pressure exerted by a PAIB on another PA to provide professional services at a fee level that does not allow for sufficient and appropriate resources to perform the services as an example of a threat to compliance with the fundamental principles.

Provisions to Enhance Transparency about Fee-related Matters, Including Auditor Communication with Those Charged with Governance (TCWG) and Public Disclosure

- Establish a requirement for firms to communicate to TCWG that the audit fees quoted will allow the firm to perform the engagement in accordance with professional standards.
- For audits of general purpose financial statements, establish provisions to ensure that the audit fee is disclosed for audit clients that are public interest entities (PIE).

Fee-dependency

Applicable to PIEs Only

- Encourage, or alternatively require, firms to disclose to TCWG if the total fees from the PIE audit client exceed the threshold set out in the Code after the first year of the engagement, and consider whether this information should be publicly disclosed.
- Strengthen the current requirement in the case of PIE audit clients by requiring the firm to determine the application of pre-issuance review as a safeguard, instead of allowing post issuance review, once total fees from a PIE client significantly exceed the threshold.

¹ In line with paragraph 400.4 of the Code, the term “firm” is used to address the responsibility of professional accountants in public practice and their firms. The term “firm” is used in accordance with the description that is in the Glossary of the Code.

- Require the firm to end the engagement if the total fees from a PIE audit client continue to exceed the established fee threshold for five consecutive years.
- Require the firm to disclose publicly each year if the PIE audit client continues to exceed the threshold set out in the Code and also the safeguard applied, until the firm is required to end the engagement.

Applicable to non-PIEs

- Encourage, or alternatively require, the firm to disclose to TCWG each year if the total fees from the non-PIE client exceed 30% of total fees of the firm after the first year of the engagement, and encourage firms to discuss with TCWG whether this information should be publicly disclosed.
- Establish a requirement for firms of non-PIE audit clients to disclose to TCWG when total fees from the client reach 30% of total fees of the firm for three or five consecutive years, and discuss with TCWG the actions that might be applied as safeguards, i.e., a pre-issuance or a post-issuance review.
- No requirement for the firm to cease to be the auditor when the fee threshold is exceeded for a specified number of consecutive years.

Other

- Consider how to engage with stakeholders through means other than the Code about the relationship between audit quality and fees (e.g., IESBA Staff Publications).

I. Introduction and Background

1. In September 2018, following the Board's consideration of the June 2018 [final report](#) of the Fees Working Group (Fees Final Report), the IESBA approved a [project proposal](#) on fees. 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 "revised and restructured Code" or the "Code") pertaining to fee-related matters. The project involves consideration of changes to the Code so that it remains robust and appropriate in enabling professional accountants to meet their responsibility to comply with the fundamental principles and, where applicable, be independent. The project proposal set out the project scope which is summarized in **Agenda Item F**.

Purpose of this Paper

2. The purpose of this paper is to present the Task Force's views and preliminary proposals. The remainder of this paper is organized as follows:
 - Section II – Level of Audit Fees
 - Section III – Fee Dependency in the Context of Audit Engagements
 - Section IV – Fee-related Safeguards
 - Appendix – Summary of Fee-related Safeguards in the Code

Matters that are Outside of the Project Scope and Interactions with Other Work Streams

Audit Firm Business Model

3. The Task Force notes calls from the PIOB and others for the IESBA to consider whether "the audit firm business model can be seen as a barrier to real independence, to the effective implementation of professional skepticism, and to audit quality."² The Fees Final Report included a recommendation that

² See February 2018 PIOB communication to the IESBA.

the IESBA Planning Committee give consideration to the IESBA initiating a dialogue with the IAASB on the topic of business model.

4. At its September 2018 meeting, the IESBA expressed a preliminary view that “audit firm business model” is a complex, multi-faceted topic and there is a need for robust engagement among many stakeholders, including firms, regulators, investors, the corporate governance community, preparers, national standard setters, the academic community and IFAC member bodies. Notwithstanding, the proposed changes to the Code as a result of this project are intended to:
 - Reinforce the responsibilities of firms and audit engagement partners, and ensure that the fees quoted for audit engagements do not affect the firm’s ability to perform audits in accordance with professional standards;
 - Enhance the transparency of fees charged for the benefit of TCWG and the public;
 - Strengthen how threats to independence created by fees charged are addressed, including fee-related safeguards.
5. The changes that are being proposed by the Task Force are expected to complement the work being undertaken by the Non-assurance Services (NAS) Task Force as well as the proposals in the International Auditing and Assurance Standards Board’s (IAASB) recently released Quality Management Exposure Drafts (EDs)³ and will establish further rigor to the responsibilities of firms and professional accountants when undertaking audit engagements.

IAASB QM EDs

6. The Task Force is conscious that its work will cover the consideration of certain issues that are currently being explored by the IAASB as part of its Quality Management EDs. For example, the IAASB’s EDs includes proposals that reinforce the firm and engagement partner responsibilities to perform audits in accordance with professional standards (e.g. see paragraphs 23 (e) of proposed ISQM 1 and paragraphs 23-26 of proposed ISA 220 (Revised)). To the extent practicable, the Task Force plans to align its proposals with those of the IAASB’s QM proposals, having regard to the feedback of respondents and IESBA’s own timeline for the fees project. To do so, the Task Force plans to work closely, when appropriate with Ms. Sylvie Soulier, the IAASB-IESBA Liaison and others, including the IESBA Senior Technical Director in accordance with the January 2018 [Operating Principles, Criteria and Other Considerations for IAASB-IESBA Coordination](#).

NAS

7. As discussed in **Agenda Item F**, the Task Force provided input on the NAS Task Force proposals in relation to fee-related matters and vice versa (e.g., see paragraph R410.21).

Stakeholder Outreach and Communication

8. Given the nature of the topic, the Task Force considers that it is important to seek input from outreach stakeholders (e.g., the IAASB, the Forum of Firms, the SMP Committee and the PAIB Committee) in order to develop and refine its proposals in advance of exposure. In general, this outreach will form part of the IESBA’s broader outreach and communication activities. Also, the Task Force will explore whether

³ IAASB’s Quality Management Exposure Drafts:

- Proposed International Standard on Quality Management (ISQM) 1, [Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements](#)
- Proposed International Standard on Auditing (ISA) 220 (Revised), [Quality Management for an Audit of Financial Statements](#) and
- Proposed ISQM 2, [Engagement Quality Reviews](#)

there is a need to target other stakeholders, and will schedule those meetings as appropriate. See also the Next Steps section of **Agenda Item F**.

9. After the finalization of this project, as part of its recommendations, the Task Force plans to suggest the IESBA consider continuing the outreach activities on fee-related matters and arrange for IESBA Staff to commission publications to highlight the changes resulting from this project, as a way to contribute to the global discussions about the relationship between audit quality and fees.

Fees Staff Publication

10. The Fees Final Report suggested, and it was supported by the IESBA and the CAG, that the June 2016 Staff Publication, [*Ethical Considerations Relating to Audit Fee Setting in the Context of Downward Fee Pressure*](#) be updated with the Code coming into effect in June 2019. As noted above, when the fees project is finalized, it might be helpful for the IESBA to commission a new Staff publication to highlight the enhanced fees provisions resulting from the fees project.

II. Level of Audit Fees

A. Current Provisions in the Code

11. Regarding the level of fees, Part 3 of the Code⁴ recognizes that the level of fees quoted might create a self-interest threat to compliance with the principle of professional competence and due care. However, the Code does not specify a requirement and the statement relates to situations in which the fees might be set at a low level.
12. In addition, in the context of audit and review engagements, Section 410 of the Code states that “the nature and level of fees or other types of remuneration might create a self-interest or intimidation threat and sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.”

B. Issues

- (i) *Enhancing Provisions Relating to the Level of Fees for Audits*
13. The project proposal explained that the Task Force would focus its efforts on examining the issues related to the level of fees for audit engagements, and would not deal with other types of engagement.⁵ Nevertheless, following the approach adopted by the Code, Task Force’s proposals apply to both audit and review engagements, unless it is otherwise stated.⁶
14. The Fees Final Report notes that there are reasonable perceptions that an unduly low level of audit fees could create threats to compliance with the fundamental principles and adversely impact audit quality. The Task Force also noted that the determination of an appropriate fee level for a particular audit engagement depends on many factors. The Task Force agrees that it is not practicable for a Code with global application to prescribe a specific fee level, not least because of anti-competition laws in many

⁴ Paragraph 330.3 A1 to 330.3 A2 state that:

- “The level of fees quoted might impact a professional accountant’s ability to perform professional services in accordance with professional standards.”
- “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.”

⁵ Paragraph 12 of the Project Proposal

⁶ In case of public disclosure of audit fees, the Task Force proposes the provisions apply only for audit engagements and not for review engagements.

jurisdictions.

15. Against this background, the Task Force has approached the issue of the level of fees from the perspective of the appropriate level of resources to perform an audit engagement in compliance with professional standards (and regulatory requirements), and not from the perspective of determining the appropriate level of fees. This approach is supported by the feedback that stakeholders provided to the IESBA as part of the fees fact-finding activities which is summarized in the Fees Final Report.

Task Force Proposal

16. The Task Force considers that the Code should include requirements to ensure that the level of fees quoted do not impair a professional accountant's ability to perform the audit services in accordance with professional standards. The Task Force believes that this requirement should be established only in relation to audit and review engagements as a matter of public interest. The Task Force considers that it would be helpful to include new application material in Section 330 to cross refer to the new requirements in Section 410.
17. The Task Force considered whether to add a provision to the Code to indicate that other services provided by the firm should not affect the audit fee quoted. The Task Force determined that such a provision was unnecessary, and would add complexity to the fee provisions in the Code. The Task Force believes that the focus of its proposed requirement should be on the audit services being performed in accordance with professional standards. Further, the Task Force is of the view that in some cases, the provision of certain other services which have a significant assurance element may allow a more efficient audit to be undertaken with a consequential impact on fees.

Matters for CAG Consideration

1. Representatives are asked for views about the Task Force's proposal for establish a requirement in Section 410 with a cross-reference in Section 330, for firms to be satisfied that the fees quoted for audit engagements do not affect the firm's ability to perform the audit in accordance with professional standards.

(ii) *Elaboration of the Responsibilities of PAPP, Including Engagement Partners*

18. The Fees Final Report included a suggestion that the IESBA should consider introducing provisions to the Code to clarify that it is the engagement partner's personal responsibility to address any threats presented by the level of fees (e.g., being able to demonstrate that sufficient resources have been assigned to the engagement). Also, in September 2018, IESBA members and CAG representatives emphasized the need to further explore how best to clarify the responsibilities for setting the level of fees, and asked that this work be coordinated with the IAASB as part of its revision to its Quality Control Standards.
19. The Task Force noted that there is a requirement in paragraph 23 of proposed ISA 220 (Revised) which states that:

"The engagement partner shall determine that given the nature and circumstances of the audit engagement (and any changes that may arise during its course), sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team by the firm on a timely basis. (Ref: Para. A53–A62, A64–A65, A68)"

Task Force Proposal

20. The Task Force considers that the Code should be explicit and is proposing that a new requirement be included to emphasize the engagement partner's responsibility to determine whether sufficient and appropriate resources (including personnel, technological and intellectual property resources) are

assigned or made available to perform the engagement irrespective of the fees quoted. This proposal is aligned to proposed ISA 220 (Revised).

21. The Task Force also proposes that the provision relating to acceptance of a new client relationship or changes in an existing engagement in the Code include, as a factor to consider, the level of fees that allows for sufficient and appropriate resources to perform the engagement.

Matters for CAG Consideration

2. Representatives are asked to consider and provide input to the following Task Force proposals:
- (a) Establish a requirement in Section 410 for the engagement partner to determine whether sufficient and appropriate resources (including personnel, technological and intellectual property resources) are assigned or made available to perform the engagement, irrespective of the fees quoted
 - (b) Enhance the current provisions related to the acceptance of a new engagement by adding, in Section 320, the level of fees as a factor for firms to consider in assessing relevant threats.

(iii) *Consideration of PAIB Responsibilities*

22. Some respondents to the IESBA [November 2017 Fees Questionnaire](#) suggested that the IESBA should consider the role of audit committees and those taking part in decisions concerning the appointment and reappointment of auditors. The Fees Final Report noted that fee-related issues could be also addressed by raising awareness among not only professional accountants in practice but also PAIBs, since TCWG often include PAIBs who are also subject of the Code. Regarding that recommendation, some IESBA members raised whether it is in the remit of IESBA to set up rules for PAIBs when they are acting in governance and management roles. IESBA members also observed that setting the level of fees is a two-sided process, and encouraged the Task Force to explore having proposals in the Code that raise awareness of the relationship between audit quality and appropriate level of fees more broadly.
23. The Task Force has considered this issue in relation to fees, but also considers that there may be benefit in IESBA exploring the broader responsibilities of PAIBs in governance and management roles and their interactions with auditors.

Provisions for PAIBs in the Code when Appointing or Reappointing auditors

24. Professional accountants as employees or contractors of an organization with responsibility of forming a decision on audit fees or taking part in the appointment of an auditor fall within the scope of Part 2 of the Code.⁷ As part of this project, the Task Force reviewed the relevant provisions of the Code in the context of the role of the PAIB's in appointing and reappointing external auditors.

Task Force proposal

25. The Task Force notes that Section 270 of the Code includes provisions that might be relevant to PAIBs, including management and TCWG in approving the fees quoted for the audit. For example, Section 270 notes that pressure exerted on, or by, a professional accountant might create an intimidation or other threat to compliance with one or more of the fundamental principles. Under Section 270, states that professional accountants shall not place pressure on others that the accountant knows, or has reason to believe, would result in the other individuals breaching the fundamental principles. The section also includes examples of situations in which pressure might result in threats to compliance with fundamental

⁷ Part 2 – Professional Accountants in Business

principles.⁸

26. The Task Force considers that the Code articulates the relevant principles and notes that Part 2 does not include an explicit reference to, or examples of, how the provision in the Code could be applied specifically in the context of setting audit fees. Given the importance of setting the appropriate level of fees, and the likelihood that doing so might create pressure to breach the fundamental principles, the Task Force proposes that the Board enhance the provisions relating to pressure in the Code by adding fee-related examples to paragraph 270.3 A3.

Matters for CAG Consideration

3. Representatives are asked for views about Task Force's proposal to add new application material, in Section 270, to signal pressure exerted by a PAIB on another PA to provide professional services at a fee level that does not allow for sufficient and appropriate resources to perform the services as an example of a threat to compliance with the fundamental principles.

(iv) *Enhanced Transparency about Fee-Related Matters*

27. Based on the project proposal, the Task Force considered the role of transparency in the context of the level of fees, especially the role of the communication with TCWG and public disclosure. For this purpose, the Task Force viewed public disclosure as a process making information related to fees publicly available for all users, and not only for TCWG. The Task Force also noted that in case of public disclosure, the desired transparency can be achieved by the information being made public by the responsible entity or by the firm.

Auditor Communication with TCWG

28. ISA 260 (Revised) requires auditors of listed entities to communicate with TCWG all relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, may reasonably be thought to bear on independence, including 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.⁹
29. The Code encourages regular communication between a firm and TCWG regarding relationships and other matters that might, in the firm's opinion, reasonably bear on independence even when not required by the Code.¹⁰

Task Force proposal

30. To enhance auditor communications with TCWG, the Task Force is proposing that the current provisions in the Code should be strengthened with a requirement for firms to communicate to TCWG about relevant fee-related information. The Task Force believes that this requirement should apply to all entities and not only listed companies as is the case in ISA 260 (Revised). The Task Force considers that communication with TCWG about the fees quoted will reinforce the firm's responsibility to perform the engagement in accordance with professional standards and better position those making assessments on the level of fees quoted for audit engagements.
31. Furthermore, the Task Force gave close consideration to whether transparency in setting fees would be enhanced if the Code also required the firm to seek concurrence from TCWG as to the level of fees quoted. The Task Force determined that on balance, enhanced auditor communication with TCWG

⁸ See paragraphs R270.2 to 270.3 A2.

⁹ ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 17(a)(i)-(ii).

¹⁰ Paragraph 400.40 A2

above the level of fees quoted would be sufficient. Nevertheless, the Task Force will seek to determine whether there are alternative views among Board members during the March 2019.

Matters for CAG Consideration

4. Representatives are asked for views about the Task Force's proposal for having a requirement in Section 410 for firms to communicate to TCWG that the audit fees quoted will allow the firm to perform the engagement in accordance with professional standards.

Public Disclosure

32. The Fees Final Report noted that some jurisdictions, such as Canada,¹¹ US¹² and the EU member countries,¹³ have established disclosure requirements with respect to audit fees, assurance fees and other audit-related fees charged. It was noted that these requirements are commonly directed to entities that are PIEs.
33. The Task Force also considered the feedback from the 2018 IESBA [global roundtables](#) which indicate that some stakeholders believe that transparency of NAS fees will help improve investor confidence and enable TCWG and others to generate the pressures necessary to change practice. Roundtable participants suggested that the IESBA should place increased focus on developing standards that enhance transparency, while at the same time taking into account the challenges that might exist in achieving such transparency, such as¹⁴ concerns related to the lack of global corporate governance requirements in order to require disclosures about fee-related matters. There were also questions about whether it is the IESBA's mandate to establish provisions relating to fee disclosure.

Task Force Proposal for Public Disclosure

34. As mentioned above, stakeholders raised a range of challenges related to IESBA establishing a requirement on public disclosure. However the Task Force is of the view that disclosure of fees to all stakeholders who are relying on an audit should be an important component of the profession's ethical standards, and that public disclosure of fees should be required for PIEs (and encouraged for non-PIEs at this time). It is noted from the fact finding activities of the Fees Final Report that the transparency of the fees quoted by professional accountants is important in dealing with the risk that a low level of fees could impair the auditor providing a high quality audit. At the same time such disclosure would discourage audit fees being set too high in a way that might be perceived to encourage the auditor to come to a particular conclusion.
35. The Task Force notes that in some jurisdictions there are laws and regulations for audited entities to disclose information on audit fees. The Task Force is of the view that ideally the disclosure would be made by the entity in the audited financial statements, however it would also be possible for fee information to be disclosed elsewhere, e.g. in the audit report or on the firm's website.
36. Consequently, the Task Force proposes that there be a requirement in the Code for firms to consider the laws and regulations governing the audit client's public disclosure of audit fees, and determine if the audit client is in compliance. In the absence of such disclosure, the firms should take steps to ensure that audit fees for audit clients that are PIEs are made public in a timely and in an accessible manner for stakeholders, whether in the audit report or through other means, e.g. on their website.

¹¹ Canada, National Instruments 52-110 *Audit Committees*

¹² US SEC Rule 17 CFR 240.14a-101, Schedule 14A, Information required in proxy statement

¹³ 2013/34/ EU Directive Article 18

¹⁴ See Agenda Item 9-A to the September 2018 IESBA Meeting, *NAS-Summary of Significant Matters from Roundtable, Working Group Assessments and Proposals*, Section III

37. As part of this requirement, the Task Force is also proposing new application material to:
- Give firms guidance on what is meant by “timely manner”, and provide a grace period (up to one month after the issuance of the audit report) for making the disclosure to occur.
 - Explain how to determine the fee amounts that should be disclosed.
38. As for the amount of fees, the Task Force believes that the disclosure should reflect the fees that have been paid or are estimated to be payable, based on the information available at the time of the disclosure.
39. Acknowledging that there are special situations in the context of group audits, the Task Force is proposing new application material to allow firms the option to disclose fee-related information for the group and the components in an aggregated basis.
40. The Task Force believes that there is merit in encouraging firms to also disclose fee-related information for audits of entities that are not PIEs given the increasing recognition being given to the importance of transparency in relation to audit fees.
41. In terms of applicability, the Task Force believes that its proposed requirement would be for audits of general purpose financial statements and that an *exception to this requirement would apply to*:
- Review engagements.
 - Financial statements are prepared in accordance with a special purpose framework, i.e., audit engagements that are subject to the provisions in ISA 800 (Revised).¹⁵
 - Audits of a single financial statement or a specific element, account or item of a financial statement, i.e., audit engagements that are subject to the provisions in ISA 805 (Revised).¹⁶
42. The Task Force will continue to liaise with the NAS Task Force in relation to the disclosure of fees. The Task Force also notes that any proposal involving a requirement for auditor disclosure of fee-related information (e.g., in the audit report) will be of interest to the IAASB and steps will be taken to consult with the Board through the usual channels.

Matters for CAG Consideration

5. Representatives are asked for views about the Task Force proposal to establish provisions for firms to take steps to ensure that the audit fee for audit of general purpose financial statements is disclosed for audit clients that are public interest entities (in Section 410).

III. Fee Dependency in the Context of Audit Engagements

Issues

43. A key aspect of the fees fact-finding initiative was to determine whether there is a relationship between fees and threats to maintaining compliance with the independence requirements with respect to the relative size of fees to the partner, office or the firm, and the extent to which partners’ remuneration is dependent upon fees from a particular client (fee dependency). The Fees Final Report indicates that most observed jurisdictions have rules or standards relating to relative size of fees that align with the provisions of the Code, however a few jurisdictions have more stringent rules.
44. As provided in the project proposal, the Task Force has reviewed the requirements and application

¹⁵ ISA 800 (Revised), *Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*

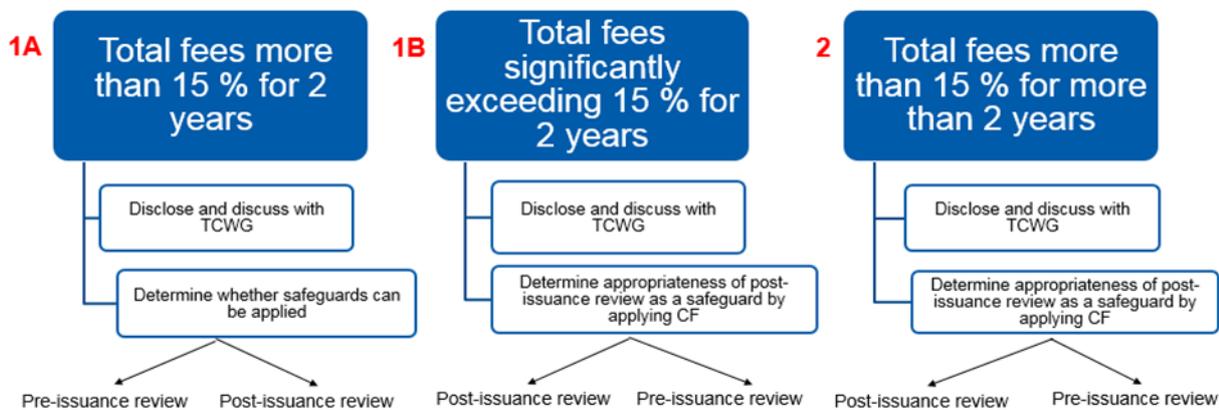
¹⁶ ISA 805 (Revised), *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*

material in the Code pertaining to fee dependency in relation to PIE and non-PIE audit clients and how threats relating to fee dependency for non-PIEs might be addressed, including for example through the use of thresholds.

Fee Dependency Provisions for PIEs

Current Provisions for PIE Audit Clients

45. The current provisions of the Code require the firm to take certain actions when an audit client is a PIE and for two consecutive years the total fees from the client and its related entities represent more than 15 percent of the total fees received by the firm expressing the opinion on the financial statements. These actions include a disclosure to TCWG, and application of certain safeguards. The Code also has different provisions for situations in which fees significantly exceed the 15 percent threshold, and if the threshold is exceeded for more than two years. The provisions are based not only for the fee for the audit client, but also for all related entities. This is expressed explicit in the requirement.¹⁷
46. The Code includes specific safeguards to address threats created by fee-dependency issues which are either a pre-issuance review or a post-issuance review of the engagement.¹⁸ The diagram below summaries the current provisions to fee dependency in the Code that apply to audits of PIEs.



Task Force Proposal

47. The Fees Final Report notes that there is little research or evidence to suggest that changing the threshold percentage for the fees charged to audit clients that are PIEs will reduce threats to independence. The Task Force notes that there was only one jurisdiction¹⁹ with a threshold that is lower than the Code (i.e., 10 percent). In June 2018 meeting, the Board expressed a preliminary view that the current threshold in the Code is appropriate. Respondents to the Fees Questionnaire did not indicate concerns about the provisions in the Code, including the safeguards. The Task Force notes that in some jurisdictions²⁰ only one example of safeguard is provided – i.e., the pre-issuance reviews. The Task Force is also of the view that once the total fees significantly exceeds the 15 percent threshold the firm should not have the discretion to determine the type of safeguard to be applied, and the Code should require the firm to apply a pre-issuance review as a safeguard.

¹⁷ Paragraph R410.4–R410.6

¹⁸ Both reviews should be performed either by a professional accountant, who is not a member of the firm (an external), or by a professional body. The pre-issuance review should be done before the issuance of the audit opinion on the second financial year, while the post issuance review is performed after the issuance of the audit opinion on the second year’s financial statements but before the issuance of the audit opinion on the financial statements for the third financial year.

¹⁹ [UK FRC's response](#) to Fees Questionnaire

²⁰ Response of the Royal Netherlands Institutes of Chartered Accountants (NBA) to Fees Questionnaire

48. The Task Force also believes the Code should also include guidance to explain how firms are to interpret and apply the word “significantly”. The Task Force proposes that a principle-based approach should be retained and that the Code should explain that firms are to use the reasonable and informed third party test²¹ in interpreting the meaning of the word “significantly.” However, the Task Force is of the view that there would be a benefit adding a threshold to the application material that would likely to require the application of the elevated actions. The Task Force proposes that this threshold should be 30 percent.
49. The Task Force reviewed whether in case of the post issuance and pre-issuance review the independence of the external professional who is required to be hired outside of the firm is appropriately addressed in the Code. The Task Force notes that according to the Glossary to the Code the term “audit team’ encompasses all those individuals who performs engagement quality control review for the engagement. Therefore, the Task Force determined that the external reviewer should be independent of the client in the same way as other audit team members.
50. The Task Force also considered the appropriateness of requiring the external reviewer to be outside of the firm. The external reviewer involved in performing the pre-issuance and post-issuance reviews in the extant Code and the *revised and restructured* Code is the same. As a consequence, when evaluating fee dependency, the total fees received from an audit client is calculated at a firm level and not at a network level, and a reviewer from another firm in the same network is considered appropriate. The Task Force concluded there is no need to change current safeguards and require the reviewer to be not only outside the firm but out of the network as well given the existing requirements in the Code, referred to above.
51. In addition to the type of safeguards, some stakeholders²² also reported that in their jurisdictions when the total fees from one client exceeds the threshold for several years, the auditor is required to end the engagement and cease to be the auditor of the entity. These national requirements are in line with the rules of the most recently adopted EU regulation²³ that also prescribes that if the fees received from a PIE client continue (after three consecutive years) to exceed 15 percent of the total fees received, the audit committee shall decide whether the auditor may continue to carry out the statutory audit for an additional period which shall not, in any case, exceed two years. That means that, in the EU, the auditor is required to end the engagement in all cases if the total fees from the client exceeds the threshold for more than 5 consecutive years.
52. The Task Force is also of the view that in case of PIE audit clients if the total fees continue to exceed the threshold, the threat cannot be addressed to an acceptable level by applications of the safeguards and the firm should be required after a certain period of time to cease to be the auditor. The Task Force notes the recently adopted rules in Europe and proposes that the Code also adopt 5 years as a maximum.
53. Besides the requirements mentioned above, the Task Force also considered the role of transparency and public disclosure and the Task Force is of the view that the public disclosure should be an important component to address the perception issue related to fee dependency and the firm should be required to disclose each year if the client continues to exceed the threshold set out for two consecutive years and also the safeguard applied. Application materials would give guidance on the way of this disclosure.
54. The Task Force also recommends that the Code includes some measures that firms could take as a first step, even after the first year to address the threats to independence created by the fee dependency from a client. The Task Force recommends that the fee dependency be communicated to TCWG and

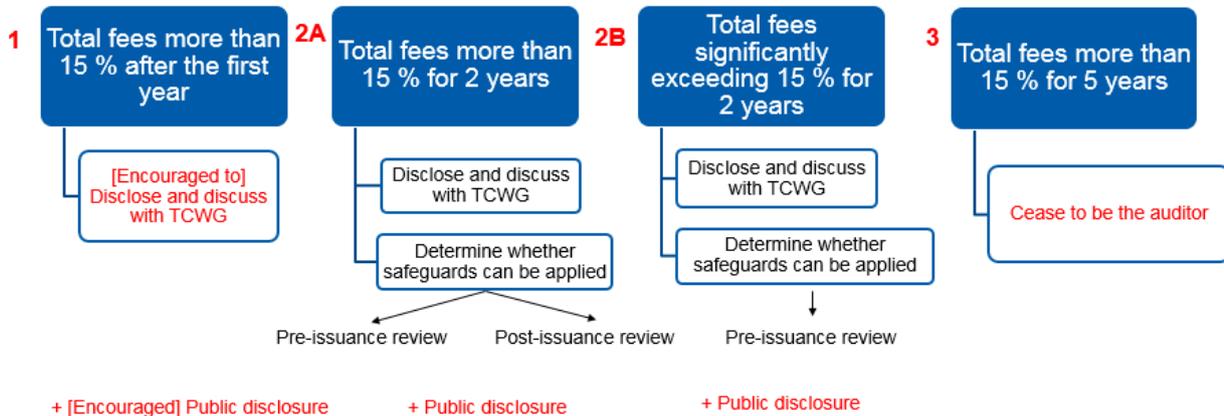
²¹ Paragraph 120.5. A4

²² UK FRC’s and NBA’s responses to Fees Questionnaire

²³ Regulation nr. 537/2014 of The European Parliament and European Council on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC, Article 4

discussed as to whether it should be made public. The Task Force asks for the Board members' input and views whether the firms should be required, or only encouraged, to apply these actions after the first year.

55. Below is a revised diagram to summarize how the provisions in the Code might be revised for PIE clients (changes to the current provisions are marked in red), including both options presented in paragraph 54 above:



Matters for CAG consideration

6. Representatives are asked for views about Task Force proposals to:
- (a) Encourage, or alternatively require, firms to disclose to TCWG if the total fees from the PIE audit client exceed the threshold set out in the Code after the first year of the engagement, and consider whether this information should be publicly disclosed
 - (b) Strengthen the current requirement in the case of PIE audit clients by requiring the firm to determine the application of pre-issuance review as a safeguard, instead of allowing post issuance review, once total fees from a PIE client significantly exceed the threshold.
 - (c) Require the firm to end the engagement if the total fees from a PIE audit client continue to exceed the established fee threshold for five consecutive years.
 - (d) Require the firm to disclose publicly each year if the PIE audit client continues to exceed the threshold set out in the Code and also the safeguard applied, until the firm is required to end the engagement.
7. Representatives are asked to consider and provide their views about whether the auditor communication with TCWG and the required public disclosure should occur immediately after the first year of the engagement; and whether it should be required; or only encouraged for audits of entities that are PIEs.

Fee Dependency for non-PIEs

Current Provisions for non-PIE Audit Clients

56. The Code sets out that if the total fees from an audit client represent a large proportion of the total fees generated by the firm expressing the audit opinion, the dependence on that client and concern about losing the client create a self-interest or intimidation threat. The Code provides factors and examples of

action that might be safeguards how to evaluate and address that threat. Also, similarly to firms, same threats are created at partner and at office level.²⁴

Type of Fees

57. The Task Force examined the type of fees that should be taken into consideration by the firm when applying this provision. The Task Force notes that the Code clearly states that a threat is created when total fees from one client represent a large proportion of the total fees from all clients of that firm. The provision does not refer exclusively only to audit fees, but includes fees from all type of services, i.e. NAS or any other type of services other than audit, provided to an audit client need to be considered once evaluating the proportion in comparison the total fees generated.

Related Entities

58. Further, the Code does not include explicitly – unlike in case of PIE clients – that the fees paid by the related entities²⁵ of the audit client form part of total fees. 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.

59. In relation to evaluation of related entities of non-listed audit clients, it is noted that the general provisions of Part 4A set out that the related entities over which the audit client has direct or indirect control should be included to the definition of audit client. Also where the audit team knows, or has reason to believe, that a relationship or circumstance involving any other related entity of the client is relevant to the evaluation, the audit team shall include that related entity as well.

60. The table below shows a clarification to the definition of audit client when evaluating fee-dependency:

<i>Non-PIE Clients</i> ²⁶	<i>PIE Clients (Listed Entities + Other PIEs)</i> ²⁷
<ul style="list-style-type: none"> • Audit client, and • Related entities over which has direct or indirect control, and • Other related entities if relevant to the evaluation of independence (by “knows or reason to believe” test). 	<ul style="list-style-type: none"> • Audit client, and • All related entities.

Task Force Proposal

61. The Task Force is of the view that in order to enhance the current provisions in the Code for non-PIE

²⁴ Paragraph 410.3 A1-A6

²⁵ An entity that has any of the following relationships with the client:

- (a) An entity that has direct or indirect control over the client if the client is material to such entity;
- (b) An entity with a direct financial interest in the client if that entity has significant influence over the client and the interest in the client is material to such entity;
- (c) An entity over which the client has direct or indirect control;
- (d) An entity in which the client, or an entity related to the client under (c) above, has a direct financial interest that gives it significant influence over such entity and the interest is material to the client and its related entity in (c); and
- (e) An entity which is under common control with the client (a “sister entity”) if the sister entity and the client are both material to the entity that controls both the client and sister entity.

²⁶ R400.20

²⁷ R400.20 and R410.4

audit clients, besides requiring firms to apply the conceptual framework, there would be a benefit in requiring firms to disclose to TCWG when total fees from the non-PIE audit client exceed a nominated threshold for a number of years, and to discuss actions that might be safeguards to address the threat created by the total fees received by the firm from the client.

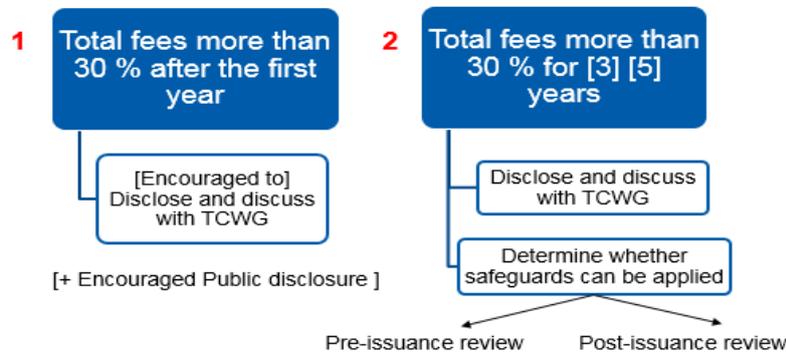
62. As a first step in determining potential thresholds for non-PIEs, the Task Force considered how best to determine the level of a threshold that would be a trigger for the firm to engage with TCWG on the firm's fee position and reassess threats. Based on the information provided by the Fees Final Report, those jurisdictions that introduced thresholds for non-PIEs adopted a variety of thresholds, such as 15 percent or 30 percent.²⁸
63. The Task Force also took into consideration views from stakeholders and IESBA members that suggested that any new provisions related to fee dependency in relation to non-PIE clients should not add additional burden on non-PIEs that are smaller entities that would not be proportionate with the intended aim of the project. Further, the Task Force recognized that it should appropriately address the situation of recently established, or new firms, with limited client bases.
64. Against the background of the above-mentioned cautions, the Task Force proposes the Board adopt a similar approach regarding the requirements and application materials for non-PIE audit clients as the Code sets out currently for PIE audit clients, but with a different threshold and number of consecutive years, and some greater latitude with safeguards than is proposed for PIEs. Therefore the Task Force suggests that the Code includes a requirement where for certain consecutive years the total fees from a non-PIE client exceeds 30 percent of fees generated by the firm expressing the opinion, the firm is required to take certain action set out by the Code. These actions are proposed to be based on the current PIE audit client model.
65. Regarding the determination of the numbers of the consecutive years after which the firms would be required to decide on application of actions that might be safeguards, and also to confirm the percentage suggested for the threshold, the Task Force anticipates further coordination and outreach with the representatives of the SME and SMP community to ask for their experiences and suggestions to this issues. In line with that, the Task Force seeks Board members' views regarding the timely manner of this requirement, whether it should be 3 years or 5 years.
66. In addition, in a similar way to that for PIEs clients, the Task Force recommends that IESBA includes provision on certain actions to be taken after the first year - and then each year - when the total fees generated from the non-PIE client exceeds the threshold set out in the Code. The Task Force also seeks the view of Board members whether these actions should be required or only encouraged. The Task Force notes, that in case of a requirement the disclosure is not suggested be part of the provision, it should be only encouraged in any cases.
67. Strengthening the Code in this respect based on the PIE model but allowing greater latitude in the thresholds and safeguards adopted would be a balanced approach bearing in mind the nature of the threats and public interest considerations. In adopting this approach, the Task Force has sought also to bear in mind stakeholder feedback from the NAS Roundtables about the positive benefits achievable through greater transparency of circumstances to TCWG and the public. The Task Force is also conscious that the Board has on its forward work program a project to review the definition of PIEs which is likely to allow the Board to consider in greater detail, if it so decides, the basis for the different approaches adopted in the Code for PIEs and non-PIEs.²⁹
68. With the above mentioned proposals, the Task Force aims to adopt similar provisions with respect to

²⁸ The reported thresholds among those jurisdictions that responded the Fees Questionnaire are the following: In Germany 30 percent, in the UK 15 percent and in the Netherlands also 15 percent.

²⁹ IESBA Strategy and Work Plan, 2019-2023

specific safeguards that currently apply to PIEs, and not require the firm to cease to be the auditor once a nominated threshold continues to be exceeded.

69. Below is the diagram presenting how the provisions in the Code proposed to be revised, including the options provided for the IESBA deliberation:



Matters for CAG consideration

8. Representatives are asked to consider and provide input to the following Task Force proposal:
- Encourage, or alternatively require, the firm to disclose to TCWG each year if the total fees from the non-PIE client exceed 30% of total fees of the firm after the first year of the engagement, and encourage firms to discuss with TCWG whether this information should be publicly disclosed.
 - Establish a requirement for firms of non-PIE audit clients to disclose to TCWG when total fees from the client reach 30% of total fees of the firm for three or five consecutive years, and discuss with TCWG the actions that might be applied as safeguards, i.e., a pre-issuance or a post-issuance review.
 - No requirement for the firm to cease to be the auditor when the fee threshold is exceeded for a specified number of consecutive years.
9. Representatives are asked to consider and provide their views on the options for the possible number of consecutive years to be applied to the threshold proposed for non-PIE audit clients.

IV. Fee-related Safeguards

Issue

70. The Appendix to this paper is a summary of the revised fee-related safeguards in the Code. In relation to the examples of fee-related safeguards involving a review by an appropriate reviewer, questions have been raised by IOSCO³⁰ and International Forum of Independent Audit Regulators (IFIAR)³¹ about whether an individual professional within a firm doing a review is an appropriate safeguard. There is a concern that the individual performing the review may be inclined to make judgments that protect the economic and other interests of the firm rather than the public interest needs of investors. This observation was also made about similar NAS-related safeguards.
71. Other suggestions made by IOSCO include that the safeguards for contingent fees in the extant Code should be added as safeguards that might address threats created by level of fees charged. These

³⁰ [Letter from IOSCO's Committee on Issuer Accounting, Audit and Disclosure; 20 March 2018](#)

³¹ [Comments on the IESBA Proposed Revisions Pertaining to Safeguards in the Code – Phase 2, May 29 2017](#)

safeguards are the following:³²

- “An advance written agreement with the client as to the basis of remuneration;
- Disclosure to intended users of the work performed by the professional accountant in public practice and the basis of remuneration;
- Quality control policies and procedures; or
- Review by an independent third party of the work performed by the professional accountant in public practice.”

Recap of IESBA’s Safeguard-Related Decisions in Finalizing the Revised and Restructured Code

72. The revised description of “safeguards”³³ in the Code emphasizes that safeguards are applied only when they are available, and capable of being applied to reduce threats to an acceptable level. The examples of actions that might be safeguards set in the Code are not intended to be all-inclusive, and are not guaranteed to be appropriate safeguards in all situations.
73. In finalizing the *revised and restructured* Code the IESBA responded to regulatory concerns about having certain conditions, policies and procedures in the Code as examples of safeguards. The Code no longer categorized these activities as safeguards and clarifies that conditions, policies and procedures are the factors that are to be considered when evaluating whether a threat is at an acceptable level. The Code also emphasizes that applying safeguards is only one of the ways to address a threat (see paragraph R120.10 of the Code).

Task Force Views

74. The Task Force notes that IOSCO’s and IFIAR’s concerns about the examples of fee-related safeguards were based on the 2016 Edition of the IESBA Handbook and did not take into account the revisions arising from the Safeguards project that now form part of the revised and restructured Code.
75. Responding to the concerns raised related to the safeguards involving a review by an appropriate reviewer the Task Force notes that, subject to approval of the proposals above, the elevated requirements and application materials provide further actions for PAPPs to address threats created by the level of fee and fee dependency. Furthermore these proposed changes also aim to
- Take into account the PIOB and regulatory concerns in relation to fees; and
 - Incorporate the principal aims of jurisdictional provisions relating to fee-dependency and independence matters in the Code.
76. Further, the Task Force is of the view that when threats to independence are created by the fees generated by a firm from an audit client that represent a large proportion of the revenue of one partner, or one office, “...having an appropriate reviewer...” including when this reviewer is an individual within the firm continues to be an appropriate safeguard.
77. The Task Force also notes that regarding the appropriate reviewer the *revised and restructured* Code introduced a provision to ensure that the individual who is an appropriate reviewer has the competence and objectivity to perform the review.³⁴

³² Extant Code, Part B, Professional Accountant in Public Practice, Section 240- *Fees and Other Type of Remunerations*, para. 240.4

³³ See paragraph 120.10 A2 for a description of safeguards.

³⁴ Paragraph 300.8 A4 sets out that an appropriate reviewer is a professional with the necessary knowledge, skills, experience and authority to review, in an objective manner, the relevant work performed or service provided. Such an individual might be a professional accountant.

Summary of Fee-related Safeguards in the Code

1. Examples of actions that might be safeguards to address **self-interest threats created by the level of fees** charged are:
 - Adjusting the level of fees or the scope of the engagement.
 - Having an appropriate reviewer review the work performed.
2. Examples of actions that might be safeguards to address **self-interest threats created by contingent fees** are:
 - Having an appropriate reviewer who was not involved in performing the non-assurance service review the work performed by the professional accountant.
 - Obtaining an advance written agreement with the client on the basis of remuneration.
3. Examples of actions that might be safeguards to address **self-interest threats created by referrals and commissions** are:
 - Obtaining an advance agreement from the client for commission arrangements in connection with the sale by another party of goods or services to the client might address a self-interest threat.
 - Disclosing to clients any referral fees or commission arrangements paid to, or received from, another professional accountant or third party for recommending services or products might address a self-interest threat.
4. Examples of actions that might be safeguards to address **self-interest or intimidation threats created** when the **total fees generated** from an audit client by the firm **represent a large proportion of the total fees of that firm**, and there is concern about losing the client is:
 - Increasing the client base in the firm to reduce dependence on the audit client.
5. Examples of actions that might be safeguards to address **self-interest or intimidation threats 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 are:
 - 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.
6. Examples of actions that might be safeguards to address **self-interest threats created by overdue fees** are:
 - Obtaining partial payment of overdue fees.
 - Having an appropriate reviewer who did not take part in the audit engagement review the work performed.