



## **PROPOSED REVISIONS TO THE FEE-RELATED PROVISIONS OF THE CODE**

Issued 4 May 2020

ICAEW welcomes the opportunity to comment on the Proposed Revisions to the Fee-related Provisions of the Code published by IESBA in January 2020, a copy of which is available from this [link](#).

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## KEY POINTS

1. We agree with the overall approach and, on the whole, the revisions proposed. We have commented on a number of aspects in our responses below to the specific questions asked,
2. The key areas where we have made alternative suggestions are in respect of:
  - a. The proposal to set a fee limit of 30% in respect of the audit of non-PIE entities. We understand the practical difficulties inherent in setting a particular limit in an international code of ethics, but we believe the prospect of losing 30% of a firm's income in one go would at the very least be perceived to result in significant threats to independence. If a lower limit cannot be set, it may be better not to specify one at all.
  - b. The proposal to require measures to be taken after the proposed limit for the audit of PIEs is exceeded for two years. We believe it would be reasonable to alert those charged with governance of a potential issue after two years but we would prefer three years to be applied before the full set of actions required are needed. There can be many good reasons why a limit could be temporarily exceeded for two years without a suggestion of a permanent issue.
  - c. The proposal to require external disclosure of a potential dependency problem after two years. As noted above, we believe three years would be more appropriate.

### Evaluating Threats Created by Fees Paid by the Audit Client

**Question 1. Do you agree that a self-interest threat to independence is created and an intimidation threat to independence might be created when fees are negotiated with and paid by an audit client (or an assurance client)?**

3. Yes: any arrangement in which a member receives remuneration from a source, where future repeat fees might depend on whether the source wishes to reappoint the member, will create a threat. It might not be a significant threat and even if it is, existing processes, requirements and safeguards will usually address it, but that is made clear in the proposed wording.

**Question 2. Do you support the requirement in paragraph R410.4 for a firm to determine whether the threats to independence created by the fees proposed to an audit client are at an acceptable level:**

- (a) Before the firm accepts an audit or any other engagement for the client; and  
(b) Before a network firm accepts to provide a service to the client?**

4. Yes: this follows from the threats and safeguards approach inherent in the IESBA Code of Ethics (the Code) and in particular the general approach to establishing auditor independence provisions.

**Question 3. Do you have views or suggestions as to what the IESBA should consider as further factors (or conditions, policies and procedures) relevant to evaluating the level of threats created when fees for an audit or any other engagement are paid by the audit client? In particular, do you support recognizing as an example of relevant conditions, policies and procedures the existence of an independent committee which advises the firm on governance matters that might impact the firm's independence?**

5. We are not sure that the Code needs every single factor that might be relevant in a particular situation to be set out as if forming a checklist. That might be appropriate for a helpsheet but in the Code, examples of types of factor are sufficient. Relevant factors will relate either to the level of fee dependency (relative size and profitability for the audit firm; method of remunerating the audit partner, etc) and the level of involvement by others independent of executive management in the fee setting process (structure of the audited entity's governance, who agrees the audit fees, etc).

6. The existence of an independent committee which advises the firm on governance matters that might impact the firm's independence is but one means of arriving at a situation where the level of the audit fee is not dependent on keeping the executive management of the audited entity happy.

#### Impact of Services Other than Audit Provided to an Audit Client

**Question 4. Do you support the requirement in paragraph R410.6 that a firm not allow the level of the audit fee to be influenced by the provision by the firm or a network firm of services other than audit to the audit client?**

7. Yes. As the Exposure Document notes, fees can be influenced by many factors so in practice it would be difficult to determine whether this requirement had or had not been complied with. However, the point made by the requirement is important and from a perception perspective, it is important to be able to illustrate that there is no clear link. This is why the requirement is already in place in the UK and the European Union.

#### Proportion of Fees for Services Other than Audit to Audit Fee

**Question 5. Do you support that the guidance on determination of the proportion of fees for services other than audit in paragraph 410.10 A1 include consideration of fees for services other than audit:**

- (a) Charged by both the firm and network firms to the audit client; and  
(b) Delivered to related entities of the audit client?**

8. Yes: this follows logically from the approach to independence followed in Part 4A of the Code. However it needs to be recognised that anything that involves firms having to assess what their networks are doing, and the related entities of the entities they audit, is going to require a significant logistical effort. A common-sense approach to application is therefore needed.

#### Fee Dependency for non-PIE Audit Clients

**Question 6. Do you support the proposal in paragraph R410.14 to include a threshold for firms to address threats created by fee dependency on a non-PIE audit client? Do you support the proposed threshold in paragraph R410.14?**

9. An international code needs to be set so as to be workable in a wide variety of jurisdictions, cultures and economies. Setting any absolute amount above or below which different actions need to be taken regardless of the circumstances, always runs the risk of failing to meet that criterion, and we understand why setting a very low threshold initially might be a problem. Nevertheless, 30% looks very high: we think the reasonable and informed third party would be likely to conclude that the prospect of losing nearly 30% of one's income in one go would constitute a significant threat to objectivity.
10. It may be better, in an international Code, not to have an absolute indicator if it cannot, due to practical considerations, be set at a lower level. This could be accompanied by off-Code 'persuasive' guidance indicating the thresholds already applied in various jurisdictions around the world. At the very least, at a 30% level, stronger safeguards are likely to be needed (see response to question 7 below).

**Question 7. Do you support the proposed actions in paragraph R410.14 to reduce the threats created by fee dependency to an acceptable level once total fees exceed the threshold?**

11. As noted in our response to question 6 above, if a specific threshold of 30% is retained we believe stronger measures would be needed. We believe that with a fee dependency at this sort of level, the actions specified in R410.14 would be needed earlier than five years – perhaps three?
12. An additional or alternative strengthening measure might include a requirement to give specific assessment to potential threats at a lower threshold (say 15%).
13. Extending the transparency measure for PIEs discussed in questions 11 and 12, to non-PIEs (adjusting for timings and thresholds) could be considered where not all shareholders are involved in governance. We accept though, that there are arguments that this could actually be counterproductive and result in increased pressure on the audit firm.

### Fee Dependency for PIE Audit Clients

**Question 8. Do you support the proposed action in paragraph R410.17 to reduce the threats created by fee dependency to an acceptable level in the case of a PIE audit client?**

14. Yes, though we think a regular period might better be considered to be three years rather than two: there can be many legitimate reasons why significant ad-hoc fees might arise in two successive years without being indicative of a regular occurrence.
15. That noted, it might be appropriate for the requirement to alert those charged with governance (TCWG), in R410.24, to be retained at two years. This would alert TCWG about a potential issue with audit reappointments in advance and allow them to request a review if the auditor has determined that it is not necessary, but they disagree.
16. We note that the engagement quality review safeguard referred to excludes the possibility of a review from someone inside the firm. We believe that it might assist some smaller firms without compromising independence if a review were consider acceptable by someone from within the firm if the degree of fee dependence was not excessive and that individual's remuneration were not dependent significantly on the same profit source as is contributed to by the fees from the audited entity.

**Question 9. Do you agree with the proposal in paragraph R410.19 to require a firm to cease to be the auditor if fee dependency continues after consecutive 5 years in the case of a PIE audit client? Do you have any specific concerns about its operability?**

**Question 10. Do you support the exception provided in paragraph R410.20?**

17. Yes, we support both the requirement and the exception. In the audit of a public interest entity, perception is of critical importance and, in the absence of extenuating circumstances, we do not believe that an extended period of perceived dependence is tenable.
18. The exception in R410.20 seems to cover necessary circumstances, though in stating that we are assuming that reasonable transitional provisions would be applied by the Board on initial application of these new requirements.

### Transparency of Fee-related Information for PIE Audit Clients

**Question 11. Do you support the proposed requirement in paragraph R410.25 regarding public disclosure of fee-related information for a PIE audit client? In particular, having**

**regard to the objective of the requirement and taking into account the related application material, do you have views about the operability of the proposal?**

19. The requirements to disclose fees for the audit and for other services has been standard practice in the European Union and in the United Kingdom for many years and we believe is wholly appropriate information to disclose to shareholders and other stakeholders with a legitimate interest in the audit financial statements.
20. The requirement in R410.25c to disclose a potential fee dependency situation is perhaps more debatable. As discussed under question 7 above, there are arguments that this and the requirement in R410.24, could actually be counterproductive and result in increased pressure on the audit firm. We understand that the rationale is that in the case of public interest entities, the corporate governance arrangements applicable would be expected to counteract this concern. On balance, therefore, we support this proposal as giving useful information to shareholders and other stakeholders with a legitimate interest in the audit financial statements, to enable them to draw their own conclusions on independence. However, if the information is being disclosed to TCWG after two years (see question 8 above), it would be reasonable for TCWG to consider what actions to take in advance of wider disclosure and therefore it might be appropriate to extend this further disclosure requirement to three years.
21. Unlike in R410.23 and R410.24, R410.25 does not clarify that it applies only to public interest entity audits. While this can be worked out from headings, it would be helpful, and enhance consistency, to include this reference.

**Question 12. Do you have views or suggestions as to what the IESBA should consider as: (a) Possible other ways to achieve transparency of fee-related information for PIEs audit clients; and (b) Information to be disclosed to TCWG and to the public to assist them in their judgments and assessments about the firm's independence?**

22. Our comments on these matters are included in the responses to the questions above.

### Anti-Trust and Anti-Competition Issues

**Question 13. Do you have views regarding whether the proposals could be adopted by national standard setters or IFAC member bodies (whether or not they have a regulatory remit) within the framework of national anti-trust or anti-competition laws? The IESBA would welcome comments in particular from national standard setters, professional accountancy organizations, regulators and competition authorities.**

23. Most of our members who carry out audits do so within the United Kingdom, where there are extensive requirements on fee dependency and transparency already. These have not caused problems with competition authorities. In past dealings with competition authorities on fee-related matters, the principal concern has been to ensure that our requirements do not prescribe specific fee rates, a matter not addressed by the Code or these proposals.

### Proposed Consequential and Conforming Amendments

**Question 14. Do you support the proposed consequential and conforming amendments to Section 905 and other sections of the Code as set out in this Exposure Draft? In relation to overdue fees from an assurance client, would you generally expect a firm to obtain payment of all overdue fees before issuing its report for an assurance engagement?**

24. Yes we support the consequential amendments. However as regards the requirement in respect of overdue fees, it needs to be borne in mind that Part 4B of the Code covers a wide range of assurance engagements and requirements need to be flexible in order to be proportionate. It would be better for discussion on overdue fees to focus on significant amounts.

***Question 15. Do you believe that there are any other areas within the Code that may warrant a conforming change as a result of the proposed revisions?***

25. No. For some jurisdictions the new proposals will have quite a significant effect already and it is best to keep changes as simple and focused as possible.