



1 March 2018

The Chairman
International Ethics Standard Board for Accountants
International Federation of Accountants
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Dear Stavros

Fees Questionnaire – Fees Charged by Audit Firms

CPA Australia represents the diverse interests of more than 163,000 members working in 125 countries and regions around the world. We make this submission on behalf of our members and in the broader public interest.

CPA Australia takes the view that there can be a correlation between fees charged for audit services and corresponding ethical and independence issues. While fees are an important factor impacting on the principle of independence, behavioural practices of accountants can be of equal or greater significance with respect to actual and perceived independence. There may in fact be a greater correlation between audit fees and audit quality as compared to audit fees and independence.

The responses to the questionnaire (see Appendix 1) are representative of views obtained from CPA Australia's member representative committees. Results and findings from CPA Australia's Quality Review Program, which provides monitoring and oversight of members' compliance with Australian Professional Standards, Australian Auditing Standards and applicable laws and regulations, indicate that the level of fees charged may be a contributing factor where breaches of independence are identified.

If you require further information on our views expressed in this submission, please contact Josephine Haste, Policy Adviser – Ethics and Professional Standards by email at josephine.haste@cpaaustralia.com.au or on +61 3 9606 9693.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Stuart Dignam', written over a horizontal line.

Stuart Dignam
General Manager - Policy & Corporate Affairs

Appendix 1

CPA AUSTRALIA RESPONSE TO IESBA FEES QUESTIONNAIRE RE LEVEL OF FEES CHARGED BY AUDIT FIRMS

Respondent Classification: IFAC Member Body

Relevant Survey Questions

Section B5 - National Standard Setters and IFAC Member Bodies

General

1. Do you believe that the level of fees charged by an audit firm gives rise to ethics and/or independence issues? Please explain your response.

CPA Australia concurs with the view that the level of fees charged by an audit firm does give rise to *both* ethical and independence issues. Accounting firms, in particular SMPs, are facing significant pressures to reduce fees across their service offering. Auditing and assurance services are sometimes used as a loss leader to allow firms to maintain clients and continue to offer more profitable services like tax or strategic planning. Furthermore, many clients view audit and assurance services as “compliance” work and therefore wish to spend as little as possible on the service. The pursuit of ancillary services may result in firms undertaking other engagements without appropriate consideration of any independence issues. As firm offerings become more commoditized and automated it is becoming more difficult for SMPs to distinguish themselves from the competition, resulting in clients looking at the service offer based on price. For many years now, the situation where members underquote audit services has been referred to as “buying the audit.” This practice often results in under-experienced, junior, relatively less expensive staff being assigned to audits to reduce the loss. This is an industry wide practice resulting in potentially deleterious consequences for audit quality and the training and development of junior audit practitioners who in future, may be responsible for signing off audits.

Cost recovery pressures may result in inappropriate time allocation or budgetary constraints which leads to a reduction of senior staff allocated to the engagement in a managerial or supervisory capacity. Once again, this can result in significant consequences for audit quality and the development of junior staff.

The above demonstrates that *both* ethical and independence issues may arise.

2. Has your organization identified from inspections, disciplinary investigations or other means, any fee-related issues that might have created threats to compliance with the fundamental principles or to independence? If so, please describe the finding. For example:

- **What was the nature of the issue?**
- **How frequently did it occur and what was the severity?**
- **Did the firm appropriately deal with the issue? If not, do you believe that there are impediments that might have affected the firm’s response, and if so, what were they?**

In Australia, the auditing standards have the force of law. This change to auditing standards has seen most practitioners resign from honorary audits as it becomes apparent that the auditing standards apply equally regardless of the type or size of the audit engagement. Most practitioners, through

targeted education, now understand that an audit of an incorporated association must be completed with the same level of professional competence and due care as a public interest entity, listed or proprietary company audit.

It is taking more time for the message to become clear to the management committees of incorporated associations. CPA Australia has been contacted by committee members of incorporated associations to recommend practitioners who will conduct an audit on an “honorary” basis.

Management of CPA Australia’s Quality Review Program (QRP) has observed a decline in members’ recorded breaches of the auditing standards. The auditing standards have been relatively stable since 2010 which has allowed practitioners the time to improve their overall audit quality. Furthermore, the introduction of mandatory registration of SMSF audit practitioners has resulted in many practitioners resigning from the discipline, especially if they conducted only a small number of SMSF audits. Overall, this initiative has resulted in positive outcomes for audit quality. In the past, independence was the primary issue to plague SMSF audit practitioners. The QRP is referring significantly less members to professional conduct for breaches of independence requirements. While the percentage of total reviews resulting in recorded breaches of the auditing standards has halved since the force of law and mandatory registrations were introduced, the QRP does observe ongoing difficulties with a percentage of SMPs in complying with auditing and assurance standards. Members often struggle to understand the expectations of the standards or requirements set by regulators.

3. Does your organization have any other concerns about the level of fees charged for audit or non-audit services? If yes, please describe them and their basis. Does your organization have any current or proposed initiatives to deal with those concerns?

CPA Australia continually engages with members on issues regarding audit and assurance services. CPA Australia shares with its members on an annual basis, breaches and observations from the QRP. The QRP and Continuing Professional Development programs reinforce that there is no tiered or differentiated approach to audit quality based on the size or type of entity being audited and that all audits must be undertaken with the same level of competence and due care. The QRP adopts an educative approach to monitoring members compliance against prescribed audit and assurance standards. This approach allows members to engage in an open dialogue with their professional body to obtain the support and guidance that is needed in their individual circumstances which enables the member to provide their clients with a technically competent, quality service that adds value to their businesses. In a small number of cases, the QRP process helps the member divest from providing audit services where the member cannot maintain the required skills or competencies, or gain an appropriate monetary return which may pose a risk to the public interest.

CPA Australia encourages members to have conversations with their clients such that they understand the time and associated costs incurred to undertake an audit. Where permitted by law or regulation, members are encouraged to examine alternative audit and assurance approaches, including reviews. While alternative services may result in a reduction in fees in the short term, the power of positive advice may hold them in good stead for future engagements or referrals from clients.

CPA Australia is not currently engaged on any specific initiatives relating to audit fees.

4. Do you believe that the IESBA Code establishes sufficient and appropriate provisions to help professional accountants and firms deal with threats to compliance with the fundamental principles and independence that might be created by the level of fees charged?

Any code of ethics which prescribes certain behaviours and conduct of members is only as strong as the professional bodies who review against the code. CPA Australia reviews members compliance across all services regardless of size or offering. At present, the extent of the review adopted by CPA Australia is far in excess of what is required by IFAC requirements.

CPA Australia's approach to quality review is to assess the policies and processes adopted by members to ensure that standards of quality and ethics are adhered to across their practices. That being said, this process is limited by the scope of the engagement, the client files that are being made available for review and the complexity of other services that are being offered by the member.

5. Do you believe that there are certain regulatory requirements in your jurisdiction relating to the level of fees charged by audit firms that are more stringent than the provisions in the IESBA Code? If so, please explain why.

The following is a summary of laws and regulations which reflect the current regulatory position for pricing and fees charged by Auditing Practitioners in Australia.

- [APES 110 Code of Ethics for Professional Accountants](#) (September 2017) issued by the APESB
 - Section 240 *Fees and Other Types of Remuneration* (applies to all public practitioners and in part refers to non-assurance services)
 - Section 290.215-290.222 *Fees* (applies to public practitioners conducting audit and review engagements)
 - Section 291.148-291.154 *Fees* (applies to public practitioners conducting other assurance engagements)
- [Australian Corporations Act 2001](#)
 - Section 331 *Fees and expenses of auditors*: "The reasonable fees and expenses of an auditor of a company are payable by the company."
"Reasonable" is not defined so as not to contravene Competition and Consumer Law.
- [Corporations Regulations 2001](#)
 - Regulation 9.2A.03 Annual statements by authorised audit company (Act s 1299G)
 - Act s 1299 (k) "a list of the 10 audits, including the approximate dollar value of the fees, for which the company has received the highest audit engagement fees in the relevant period."
- [INFO 196 Audit quality - The role of directors and audit committees](#) issued by the Australian Securities and Investments Commission (ASIC) – discusses what matters should be considered when setting audit fees

The Code of Ethics for Professional Accountants in Australia (APES 110) provides an additional requirement in relation to threats to independence which may arise from multiple referrals from one source which reads:

APES 110, AUST 290.215.1

"In certain circumstances, another party or Firm may refer multiple Audit Clients to a Firm. In these circumstances, when the total fees in respect of multiple Audit Clients referred from one source represent a large proportion of the total fees of the Firm expressing the audit opinions, the dependence on that source and concern about losing those clients creates a self-interest or intimidation threat.

The significance of the threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an Acceptable Level. Paragraph 290.215 provides examples of factors that may affect the significance of the threat and potential safeguards.”

In addition, the *Corporations Regulations 2001* in Australia, Regulation 9.2A.03(k), requires annual statements by authorised audit company (see *Corporations Act 2001*, s 1299G) to include a list of the 10 audits, including the approximate dollar value of the fees, for which the company has received the highest audit engagement fees in the relevant period. Annual statements are required to be lodged with the Australian Securities and Investments Commission (ASIC). This requirement relates to disclosure to the regulator but does not restrict the level of fees charged or proportion of fees charged to a client and its related entities.

6. What do you believe should be done to respond appropriately to concerns about the level of fees charged by audit firms? What should be IESBA’s role? Who else should play a role and what should that role be?

CPA Australia encourages IESBA to play an active role in working with professional bodies and regulators to support consistent harmonisation of legislation / regulatory frameworks and development of professional competencies.

The promulgation of standards alone is not sufficient to meet the challenges faced by SMPs who need practical guidance and case studies. Guidance material and case studies which can be customised by professional bodies will assist the profession to enhance the competencies of professional accountants when managing potential conflicts with respect to audit fees and the corresponding consequences for audit quality and independence.

Consideration could be given to the appropriateness of practitioners preparing an annual statement which requires the practitioners to prepare a quantitative and qualitative analysis of the engagements with audit clients. This analysis may require the practitioner to provide mitigating factors which provide protection for adherence with the fundamental principles as well as reasoned judgements for any deviations from researched benchmarks with respect to audit and non-audit fee revenue.

7. In your jurisdiction, are there specific regulatory provisions that apply to the level of fees charged for (a) audit and assurance engagements; and (b) non-audit services provided to audit and assurance clients?

There are no regulatory provisions that apply to setting the level of fees charged to audit and assurance clients. The *Corporations Act 2001* requires under s.331 “The reasonable fees and expenses of an auditor of a company are payable by the company.”

Laws exist to prevent businesses from engaging in conduct which may lessen competition and efficient operation of free market forces. These provisions apply to all product and service providers.

Section 45 of the Competition and Consumer Act 2010 prohibits contracts, arrangements, understandings or concerted practices that have the purpose, effect or likely effect of substantially lessening competition in a market, even if that conduct does not meet the stricter definitions of other anti-competitive conduct such as cartels.

Cartels are businesses that make agreements with their competitors to fix prices, rig bids, share markets or restrict outputs are breaking laws and stealing from consumers and businesses by inflating prices, reducing choices and damaging the economy.

It is against the law for businesses to fix prices, restrict outputs or allocate customers, suppliers or territories.

A business with a substantial degree of power in a market is not allowed to engage in conduct that has the purpose, effect or likely effect of substantially lessening competition in a market. This behaviour is referred to as 'misuse of market power'. It is not illegal to have, or to seek to obtain market power by offering the best products and services.

8. In your opinion, would a high ratio of non-audit fees to audit fees charged to an audit or assurance client create threats to an auditor's compliance with (Please select one or more answers):

- ✓ Professional competence and due care as defined by the IESBA Code?
- ✓ The other fundamental principles that are included in the IESBA Code – integrity, objectivity, professional behavior and confidentiality?
- ✓ Independence as defined by the IESBA

This analysis needs to be taken a step further, as an assessment would need to be made regarding the total fees paid by the client as compared to the total fee review of the firm. While a high ratio of non-audit fees to audit fees may pose an initial assessment of increased risk, if the overall fee revenue from that client was insignificant, then this increased risk to the fundamental principles may be reduced.

9. In your opinion, would a professional accountant's or the firm's compliance with one of the following be impacted if a high percentage of that firm's revenue is generated from providing non-audit services to the firm's clients (Please select one or more answers):

- ✓ Professional competence and due care as defined by the IESBA Code?
- ✓ The other fundamental principles that are included in the IESBA Code – integrity, objectivity, professional behavior and confidentiality?

Please refer to above explanation for determining the weighted importance of the client overall having an impact on the ratio of audit fees to non-audit fees.