

## Exposure Draft

January 2020

*Comments due: May 4, 2020*

*International Ethics Standards Board  
for Accountants®*

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# Proposed Revisions to the Fee-related Provisions of the Code

**IESBA**

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## About the IESBA

The [International Ethics Standards Board for Accountants](#)® (IESBA®) is an independent global standard-setting board. The IESBA's mission is to serve the public interest by setting ethics standards, including auditor independence requirements, which seek to raise the bar for ethical conduct and practice for all professional accountants through a robust, globally operable [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#) (the Code).

The IESBA believes a single set of high-quality ethics standards enhances the quality and consistency of services provided by professional accountants, thus contributing to public trust and confidence in the accountancy profession. The IESBA sets its standards in the public interest with advice from the IESBA Consultative Advisory Group (CAG) and under the oversight of the Public Interest Oversight Board (PIOB).

The structures and processes that support the operations of the IESBA are facilitated by the International Federation of Accountants® (IFAC®).

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## REQUEST FOR COMMENTS

This Exposure Draft, *Proposed Revisions to the Fee-related Provisions of the Code*, was developed and approved by the IESBA.

The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form. Comments are requested by **May 4, 2020**.

Respondents are asked to submit their comments electronically through the IESBA website, using the "[Submit a Comment](#)" link. Please submit comments in both PDF and Word files. Also, please note that first-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website. Although the IESBA prefers that comments are submitted via its website, comments can also be sent to Ken Siong, IESBA Senior Technical Director, at [KenSiong@ethicsboard.org](mailto:KenSiong@ethicsboard.org).

This publication may be downloaded from the IESBA website: [www.ethicsboard.org](http://www.ethicsboard.org). The approved text is published in the English language.

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

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# EXPLANATORY MEMORANDUM

## I. Introduction

1. This memorandum provides background to, and an explanation of, the proposed revisions to the fee-related provisions of the Code.
2. The IESBA approved the proposed changes for exposure at its December 2019 meeting.

## II. Background and Overview

3. In its Strategy and Work Plan 2014-2018, the IESBA committed to undertaking work to further understand a number of fee-related matters raised by the regulatory community. In addition, the IESBA committed to responding to the Public Interest Oversight Board (PIOB) who, in approving the IESBA's April 2015 pronouncement, [Changes to the Code Addressing Certain Non-Assurance Services Provisions for Audit and Assurance Clients](#), had asked the IESBA to revisit issues on auditor independence and "non-audit services" more broadly, including fee-related matters.
4. Against this background, the IESBA decided to bring forward its Fees initiative and:
  - Established the Fees Working Group in July 2015;
  - Commissioned the IESBA Staff publication, [Ethical Considerations Relating to Audit Fee Setting in the Context of Downward Fee Pressure](#), that was released in January 2016, as a first step in addressing the topic; and
  - Approved, at its March 2016 meeting, the terms of reference for the Working Group setting out the scope and focus of, and approach to, its fact-finding activities.
5. The Working Group's fact-finding activities included:
  - (a) An overview of the relevant fee provisions in a number of the G-20 jurisdictions;
  - (b) A review of relevant academic research and other literature;<sup>1</sup> and
  - (c) Outreach to stakeholders to obtain their perspectives about fee-related matters ([Fees Questionnaire](#)).<sup>2</sup>
6. At its June 2018 meeting, the IESBA was presented with the final report of the Working Group ([Fees Final Report](#)), including recommendations for the IESBA's consideration, with respect to the following focus areas:
  - (a) Level of audit fees for individual audit engagements (level of fees);
  - (b) Relative size of fees to the partner, office or the firm,<sup>3</sup> and the extent to which partners' remuneration is dependent upon fees from a particular audit client (fee dependency);

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<sup>1</sup> The IESBA commissioned an academic, Prof. David Hay, to undertake a review of relevant academic and other literature.

<sup>2</sup> In November 2017, a questionnaire was distributed to stakeholders, with a response period until March 1, 2018. Responses were received from [73 respondents](#) representing a diverse group of stakeholders from many jurisdictions.

<sup>3</sup> In accordance with the Glossary of the Code, in this paper the term "firm" comprises:

- (a) A sole practitioner, partnership or corporation of professional accountants;
- (b) An entity that controls such parties, through ownership, management or other means; and
- (c) An entity controlled by such parties, through ownership, management or other means.

- (c) The ratio of non-audit services fees to audit fees paid by an audit client;
  - (d) The provision of audit services by a firm that also has a significant non-audit services business (business model); and
  - (e) Fee-related safeguards in the Code.
7. In September 2018, pursuant to the Working Group's final report, the IESBA approved the [Fees Project Proposal](#). The project involves consideration of enhancements to the fee-related provisions of the Code so that they remain robust and appropriate in enabling professional accountants to meet their responsibility to comply with the fundamental principles and be independent.

#### **A. Current Fee-related Provisions of the Code**

8. Section 330 of the Code<sup>4</sup> provides application material on how to address a self-interest threat to compliance with the fundamental principles relating to the level of fees, contingent fees, referral fees and commissions.
9. Regarding the level of fees, Section 330 states that the level of fees quoted might impact a professional accountant's ability to perform professional services in accordance with professional standards. The Code acknowledges that a professional accountant might quote whatever fee is considered appropriate. However, it also makes clear that 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. The Code also specifies factors to evaluate the level of such a threat and provides examples of actions that might be safeguards to address this threat.
10. The International Independence Standards (IIS) set out that the nature and level of fees or other types of remuneration might also create a self-interest or intimidation threat to independence. Both Parts 4A (Section 410<sup>5</sup>) and 4B (Section 905<sup>6</sup>) of the IIS include requirements and application material related to the relative size of fees, contingent fees and overdue fees from an audit or assurance client.

#### **B. Highlights of Proposed Revisions**

11. Following detailed consideration of the issues and the existing provisions, the IESBA is proposing revisions to the Code which include modifications to:
- Articulate and address the issue of threats to independence created when fees are negotiated with and paid by the audit or assurance client.
  - Clarify that the audit fee should be a standalone fee within the spectrum of total fees from the audit client so that the provision of services other than audit does not influence the level of the audit fee.
  - Provide guidance for firms to evaluate and address the threats to independence created when a large proportion of total fees charged by the firm or network firms to an audit client is for services other than audit.

<sup>4</sup> Section 330, *Fees and Other Types of Remuneration*

<sup>5</sup> Part 4A – Independence for Audit and Review Engagements, Section 410, *Fees*

<sup>6</sup> Part 4B – Independence for Assurance Engagements Other than Audit and Review Engagements, Section 905, *Fees*

- Enhance the provisions regarding fee dependency both when audit clients are public interest entities (PIEs) and when they are non-PIEs, including establishing a threshold for addressing threats in the case of non-PIE audit clients.
- Require the firm to cease to be the auditor for a PIE audit client if circumstances of fee dependency continue beyond a certain period.
- Enhance transparency with regard to fee-related information for PIE audit clients to assist those charged with governance (TCWG) and the public in forming their views about the firm's independence.
- Enhance the robustness of guidance in the Code regarding factors to evaluate the level of the threats created when fees are paid by an audit or assurance client and safeguards to address such threats.

### C. Interactions with Current and Future IESBA Work Streams

#### *Non-assurance Services (NAS) Project*

12. The IESBA's Fees project is linked to its NAS project, which is addressing broad stakeholder concerns about auditor independence when providing NAS to audit clients. At its December 2019 meeting, the IESBA also approved an [Exposure Draft: Proposed Revision of the Non-Assurance Services Provisions of the Code](#).
13. The IESBA has closely coordinated the changes being proposed by the Fees and NAS projects, particularly in relation to (a) proportion of fees for services other than audit to audit fees, and (b) enhanced transparency of fee-related matters to TCWG. In addition, the timelines for the NAS and Fees projects are aligned.

#### Audit Quality and Auditor Independence

14. Some stakeholders have questioned whether the IESBA has a role to play in responding to broader concerns about audit quality and auditor independence relating to the multi-disciplinary business model of firms that includes the provision of audit services together with consulting and advisory services to a wide array of clients.
15. The Fees and NAS projects are not intended to expressly deal with these concerns as such concerns extend beyond the IESBA's mandate and would require multi-stakeholder dialogue. Nevertheless, the two projects include proposals that strengthen the IIS with the introduction of additional provisions relating to independence of mind and independence in appearance in an explicit manner. For example, the Fees and NAS projects:
  - Introduce proposed new requirements for firms to improve communications about fee- and NAS-related matters to TCWG and to the public in the case of audit clients that are PIEs. The IESBA believes that improved communication and transparency will assist to better inform stakeholder perspectives about auditor independence.
  - Build on and complement the provisions in Parts 1 to 3 of the Code that help with compliance with the fundamental principles, including integrity and objectivity. For example, the NAS proposals include new application material in Section 600<sup>7</sup> to emphasize that the level and the

<sup>7</sup> Section 600, *Provision of Non-assurance Services to an Audit Client*

nature of the fee charged for a NAS provided to an audit client is a relevant factor in identifying and evaluating threats to independence.

16. The IESBA believes that the proposed changes to the Code as a result of the Fees and NAS projects will strengthen the IIS and contribute towards responding to some of the concerns about the multi-disciplinary business model of firms.

*Project on Definitions of Listed Entity and PIE*

17. Some fee-related provisions of the Code (specifically, provisions relating to fee dependency) are already more stringent in the case of audit clients that are PIEs than in the case of non-PIEs. Recognizing that stakeholders have heightened expectations regarding a firm's independence when an audit client is a PIE, the IESBA agreed to maintain this pre-existing distinction in Section 410 of the Code.
18. As part of its Strategy and Work Plan 2019-2023, the IESBA has committed to revisit the current definition of PIE<sup>8</sup> (as well as the definition of listed entity) in the Code. As the NAS and Fees projects advanced, however, it became apparent that the timeline for the review of these definitions needed to be accelerated to provide clarity about the scope of entities that would be impacted by the proposed changes. Accordingly, the IESBA approved a [project proposal](#) in December 2019 and agreed to coordinate its work on this new project (PIE project) closely with the International Auditing and Assurance Standards Board (IAASB), given that concepts that underlie the definition of a PIE in the Code are also relevant to the term “entity of significant public interest” in the IAASB’s extant or proposed standards.
19. The IESBA has committed to coordinating its PIE project with the NAS and Fees projects and will consider in due course what the formulation of the effective dates of the revised provisions arising from the three projects should be to provide an appropriate transition for adoption and implementation of the changes.

**D. IAASB-IESBA Coordination Matters**

20. Some of the proposed changes to the Code in this Exposure Draft relate to, or overlap with, requirements and application material set out in the IAASB’s International Standards on Auditing (ISAs). Accordingly, the IESBA has engaged closely with the IAASB to ensure that the proposed changes are consistent or otherwise interoperable with the ISAs. As part of their coordination efforts, the IESBA and IAASB addressed the following matters:<sup>9</sup>
  - (a) Communication with TCWG regarding fee-related matters;
  - (b) Public disclosure of fee-related information in the audit report in those instances when the firm

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<sup>8</sup> The Code defines a PIE as follows:

- (a) A listed entity; or
- (b) An entity:
  - (i) Defined by regulation or legislation as a public interest entity; or
  - (ii) For which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation might be promulgated by any relevant regulator, including an audit regulator.

<sup>9</sup> At its September 2019 meeting, the [IAASB discussed the identified proposals of the IESBA Fees Task Force](#) and deliberated the potential implications the IESBA’s proposals might have for the ISAs.



considers the audit report as a suitable location for these disclosures; and

- (c) Public disclosure of audit fee-related information in the context of an audit of group financial statements (“group audit”).

The outcomes of these coordination efforts are summarized in the relevant subsections that follow.

### III. Significant Matters

#### A. Threats to Independence Created by Fees Paid by the Audit Client

##### *Inherent Self-Interest Threat Created by Fees Paid by the Audit Client*

21. In addition to any self-interest threat to compliance with the fundamental principles as covered in Section 330 of the Code, the IESBA believes that potential threats to independence also need to be considered when fees for professional services are negotiated with and paid by the client.
22. While payment of fees by an audit client to a firm is a practice that is generally recognized and accepted by intended users of financial statements, the IESBA believes that such practice creates a self-interest threat and might create an intimidation threat to independence. The IESBA's view that a self-interest threat exists is based on the risk inherent whenever the party responsible for the subject of an examination directly pays the examiner. The IESBA therefore proposes that the Code should recognize the inherent self-interest threat in the audit client payer model. (See paragraphs 410.3 A1 and 410.4 A1.)
23. The IESBA, however, believes that compliance with professional standards, including ethics requirements, is an important factor that acts to mitigate the threat and firms might often conclude that the level of the threat is at an acceptable level.
24. The proposals do not specifically address payment by another party given that this is relatively rare in practice. The IESBA notes, however, that if the parties agree that the professional service to the audit client will be carried out for no fee (“pro bono”), this does not create a self-interest threat to independence. Nevertheless, there might be such a threat in relation to compliance with the fundamental principles (as outlined in Section 330), especially with regard to the principle of professional competence and due care. In addition, other possibly related facts and circumstances, such as relationships between the stakeholders of the audited entity and the auditor, might create threats to either independence or compliance with the fundamental principles, which should be addressed in accordance with the conceptual framework.
25. With its proposals, the IESBA does not intend to suggest changes to the current business model for audit engagements, which would go beyond its mandate. The IESBA aims to raise firms' awareness of the inherent self-interest threat and other threats that might be created; and to provide guidance on how to evaluate and address threats when they are not at an acceptable level.

##### Terminology and Fee Arrangements

26. Consistent with paragraph 400.2 of the IIS which states that the term “audit” applies equally to “review,” the IESBA proposes to make clear that the term “audit fees” in the proposals refers to fees or other types of remuneration for an audit or review of financial statements. To distinguish circumstances where the proposals make specific reference to the fee for the audit of the financial statements only (i.e., not including a review of the financial statements or an audit of special purpose financial statements), the IESBA proposes that the term “fee for the audit of the financial statements” be used. (See paragraph 410.3 A3.) Also, to capture fees for all types of professional service other

than an audit or review of financial statements, the proposals refer to fees for services other than audit (i.e., assurance services other than audits and reviews of financial statements, and non-assurance services).

27. As fee arrangements and methods of payment vary widely in practice, the proposals do not explicitly specify whether firms should consider fees quoted, charged or paid when identifying, evaluating and addressing threats to independence. The IESBA also believes that it would not be appropriate for the Code to provide a detailed discussion of the possible types of remuneration a firm may receive from an audit client for professional services rendered. Instead, appropriate professional judgment should be exercised in the circumstances.

*Evaluation of Threats to Independence*

28. Given the premise that a self-interest threat to independence is created and an intimidation threat might be created when fees are negotiated with and paid by the audit client, the proposals include a requirement for a firm to determine whether such threats to independence are at an acceptable level before the firm or a network firm accepts an audit or any other engagement. In addition, as fees charged to the audit client could change after the acceptance of the engagement and therefore affect the level of the threats, if there is such change during the period of the audit engagement, the IESBA proposes that the firm be required to re-evaluate the threats. This re-evaluation is necessary, and in addition to the requirement in paragraph R120.9 of the Code to re-evaluate threats when facts and circumstances change, because the change in the fees charged occurs *after* the engagement has been accepted. (See paragraph R410.4.)

Factors Relevant to Evaluation of Level of Threats

29. To assist the evaluation of the level of the threats created when fees for an audit or other engagement are paid by the audit client, the IESBA is proposing guidance setting out various factors to consider (see paragraph 410.4 A2). Importantly, as noted above, the IESBA believes that compliance with professional standards assists in mitigating the level of the threats. In particular, the IESBA is proposing to explicitly recognize the existence of a quality management system designed and implemented by the firm in accordance with [proposed] ISQM 1<sup>10</sup> as a factor relevant in evaluating the level of threats created by fees paid by an audit client. However, as the existence of such a quality management system can be a factor relevant to a wider spectrum of issues than just fee-related matters, the IESBA believes that it should be better recognized as part of conditions, policies and procedures in Section 120.<sup>11</sup> (See paragraphs 120.12 A3 and 410.4 A3.)
30. The IESBA welcomes stakeholders' views as to whether there are other factors that might usefully be recognized in the evaluation of the level of the threats. For example, based on current practice in some jurisdictions, the IESBA considered the existence of an independent committee of the firm advising on governance matters that might impact a firm's independence (such as the remuneration of audit engagement partners in a multi-disciplinary firm that provides both audit services and services other than audit). There were views within the IESBA that inclusion of this example as a factor would go beyond the remit of this project as the existence of such a committee would depend

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<sup>10</sup> 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 ISQM 1 is anticipated to be finalized by the IAASB by Q2 2020.

<sup>11</sup> Part 1 – Complying with the Code, Fundamental Principles and Conceptual Framework, Section 120, *The Conceptual Framework*, Paragraph 120.8 A2

on the firm's corporate governance structure. The IESBA would welcome stakeholders' views as to whether the proposals should recognize this and other factors in evaluating threats created by the audit client payer model.

#### Circumstances that Impact the Evaluation of the Level of Threats

31. Taking into account the various fee-related factors proposed as well as the existence of conditions, policies and procedures as noted above, the IESBA is of the view that in practice firms might often conclude that the threats to independence created by the fees paid by the audit client are at an acceptable level.
32. However, there might be certain circumstances where the level of the threats created by the fees paid by the audit client is less likely to be at an acceptable level. The proposals explicitly identify such circumstances in Section 410 as being those relating to the level of audit fees, the proportion of fees for services other than audit to the audit fee, overdue fees and fee dependency. For each of those circumstances, the proposals set out further factors relevant to evaluating the level of threats as well as examples of actions that might be safeguards to address such threats, or what other action should be taken if no safeguards are available and capable of being applied. (See paragraph 410.4 A4.)

#### **B. Level of Audit Fees**

33. The Fees Final Report noted 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. In considering whether further enhancement to the Code might be appropriate concerning the matter of the level of audit fees, the IESBA took into consideration the difficulty of setting the level of audit fees at a global level as determining the level of audit fees that would be "right" for a given audit engagement will vary from jurisdiction to jurisdiction and depend on a variety of factors. Further, there would be a risk of breaching anti-competition laws.
34. Against this background, the IESBA considered approaching this issue not from the perspective of determining the appropriate level of audit fees but from the perspective of ensuring that sufficient and appropriate resources to perform the audit engagement are assigned or made available in compliance with professional standards. However, the IESBA recognized that this would be addressed through the IAASB's current projects to develop proposed ISQM 1 and ISA 220 (Revised).<sup>12</sup>
35. Instead, to recognize that unduly low or unduly high fees can impact the level of the self-interest threat and might create an intimidation threat to independence, the IESBA is proposing to include in Section 410 additional factors relevant to the evaluation of the threats, as well as examples of actions that might be safeguards. (See paragraphs 410.5 A2-A3.)

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

36. When entering into discussions or negotiations on audit fees and fees for services other than audit with an audit client, there are many factors that could influence the total fees charged for that particular client. The proposals acknowledge that the quantum of these fees is a business decision and firms can quote or charge whatever fees are considered appropriate (see paragraph 410.5 A1).
37. Nevertheless, the IESBA believes it is in the public interest to make clear in the Code that the fee for

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<sup>12</sup> Proposed ISA 220 (Revised), *Quality Management For an Audit of Financial Statements*

an audit engagement is a standalone fee and that it should not be considered as part of a spectrum of fees that might be charged to the audit client. Stated differently, the provision of other services by the firm or a network firm to the audit client should not influence the audit fee. (See paragraph R410.6.)

38. Notwithstanding the above, the IESBA proposes to explicitly acknowledge that paragraph R410.6 is not intended to prohibit any cost savings that can be achieved through the experience derived from the provision of services other than audit to the audit client. (See paragraph 410.6 A2.)

### **C. Proportion of Fees for Services Other than Audit to Audit Fee**

39. The Fees Final Report noted that there is a reasonable perception that a high ratio of fees for services other than audit to audit fees creates threats to independence (particularly, threats to independence in appearance). Many jurisdictions have specific rules, mainly for PIEs, related to disclosure of fees or communication with TCWG (including audit committee pre-approval of non-audit services). In addition, some jurisdictions have introduced a cap for non-audit services fees in relation to audit fees to address the threats to independence.

#### *Threshold vs Principles-based Approach*

40. As part of the NAS Project, informed by the [feedback](#) from the participants at the four global roundtables<sup>13</sup> organized in relation to that project, the IESBA considered fee restrictions in relation to NAS, including whether to require firms to cease providing further NAS to an audit client once NAS fees exceed a threshold in relation to the audit fee (i.e., a fee cap). Roundtable participants, with the exception of some regulatory participants, expressed little or no support for establishing fee caps in the Code. Taking into account this input and the fact that the Code is a body of standards intended for global application, the IESBA agreed that it would not be appropriate to establish a fee cap in the Code.
41. Within the Fees project, the IESBA explored whether to use a threshold not as a limit to the further provision of NAS, but as a trigger for a re-evaluation of the threats to independence (similar to the approach the extant Code takes in relation to the fee dependency issue with respect to PIE audit clients). As the proportion of fees would be determinable also at a network level, the calculation of the exact ratio of fees for services other than audit to the audit fee would be a complex task, and firms might not be able to obtain all the necessary information in a timely manner. On balance, the IESBA is of the view that the Code should take a principles-based approach and provide the flexibility for firms to evaluate the threats created by the proportion of fees for other services delivered throughout the period during which independence is required.
42. The IESBA therefore proposes that Section 410 first recognize that the evaluation of the level of the self-interest threat might be impacted when a large proportion of fees charged by the firm or network firms to an audit client is generated by providing services other than audit to the audit client, due to concerns about the potential loss of either the audit engagement or the other services. Such a situation might also create an intimidation threat. An additional consideration would be a perception that the firm or network firm focuses on the non-audit relationship, which might create a threat to the auditor's objectivity. (See paragraph 410.10 A1.)
43. The IESBA also proposes relevant factors to consider in evaluating the level of the threats, as well

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<sup>13</sup> The IESBA's roundtables were held in Washington, DC, U.S.A.; Paris, France; Tokyo, Japan; and Melbourne, Australia in June/July 2018.

as an example of an action that might be a safeguard (see paragraphs 410.10 A2-A3).

44. For the avoidance of doubt, the IESBA intends that the related entity provision of the Code (paragraph R400.20) would apply in determining the fees for other services provided to the audit client, i.e., services provided to related entities of the audit client would be included.
45. As part of possible other actions to mitigate such threats in relation to PIEs, the IESBA is also proposing specific disclosure of fee-related information both to TCWG and publicly. However, in considering those disclosure proposals, the IESBA was mindful of the practicalities of obtaining and disclosing such information. In particular, for confidentiality or other reasons, it might not be feasible to obtain information in relation to entities that are not controlled by the audit client. Also in order to provide a consistent reference point – particularly for public disclosure – the IESBA considered it was best to propose using the fees for other services charged during the period covered by the financial statements. (See paragraphs R410.23(a), 410.23 A1 and R410.25(b).)

#### **D. Fee Dependency**

##### *Current IIS Provisions on Fee Dependency*

46. Both Parts 4A and 4B of the IIS address fee dependency on an audit or assurance client, respectively. In Part 4A, the Code states that when the total fees generated from an audit client by a firm 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 (a similar provision is in Part 4B with respect to an assurance client). The Code also states in Part 4A that a self-interest or intimidation threat is 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 (a corresponding provision exists in Part 4B but limited to an individual partner).
47. In addition, for audit engagements, the Code includes disclosure requirements for firms and specific actions<sup>14</sup> that might be safeguards for situations in which the audit client is a PIE, and the total fees received from the client and its related entities are greater than 15 percent of the firm's total fees for two consecutive years.
48. In line with the provisions of the Code, the proposals address fee dependency as a specific circumstance that impacts the evaluation of the self-interest threat and that also creates an intimidation threat. Furthermore, informed by the Fees Final Report, the IESBA considered the opportunity for enhancing the application material relating to fee dependency, including whether there is a case for having a threshold for non-PIEs.

##### *Fee Dependency in the Case of Audit Clients that Are PIEs*

##### **Required Actions**

49. Based on the fact-finding activities underpinning the Fees Final Report, the IESBA is not aware of any specific evidence or signal that would suggest a need to revisit the current 15 percent threshold in the Code regarding fee dependency with respect to an audit client that is a PIE.

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<sup>14</sup> (i) Disclosure to TCWG; (ii) Discussion with TCWG whether a pre-issuance review or a post-issuance review performed by a professional accountant who is not a member of the firm or by a professional body might be a safeguard to address the threat and, if so, apply it. (See paragraph R410.4 of the Code.)

50. The IESBA remains of the view that communication with TCWG about fee dependency is an important action to mitigate threats created by fee dependency (see paragraph R410.24).<sup>15</sup> As TCWG have an important role to play in appointing the auditor, the IESBA believes that if the total fees from the audit client will, or are likely to, exceed the 15 percent threshold, this should be communicated with TCWG even in the first year. Nonetheless, the IESBA does not intend to change the current model regarding requiring action to be taken to address the threats only when the threshold will be exceeded for two consecutive years.
51. If fee dependency continues in the second year of the audit engagement, the IESBA proposes to require firms to determine whether a review prior to the audit opinion being issued on the second year's financial statements (i.e., pre-issuance review) would be a safeguard and, if so, apply it. (See paragraph R410.17.) The IESBA considered that in the case of PIE audit clients, a review performed after the issuance of the audit opinion on the second year's financial statements would no longer be an appropriate safeguard to reduce the threats to an acceptable level.
52. The IESBA proposes that the pre-issuance review be equivalent to an engagement quality review and be performed by a professional accountant who is not a member of the firm expressing the opinion on the financial statements.<sup>16</sup> In relation to this proposal, IESBA notes that the definition of the term "engagement quality control review" in the Code will need to be updated based on the proposed definition in ISQM 2<sup>17</sup> for the revised term "engagement quality review."
53. The extant Code also includes a pre-issuance review performed by a professional body as an alternative. The IESBA considered that whilst that safeguard might be effective, a review performed by a professional body prior to the audit opinion being issued is unlikely to be practical given timing issues and the liability risk that the professional body would likely assume in such circumstances.
54. The IESBA is of the view that the pre-issuance review as a safeguard would not be necessary if the audit is carried out by two or more firms, provided that each firm performs sufficient work to take full individual responsibility for the audit opinion and at least one firm does not exceed the 15 percent threshold. (See paragraph R410.18.) Given differences in understanding of what a 'joint audit' entails from jurisdiction to jurisdiction, the proposals do not aim to introduce or define the term 'joint audit' in the Code. They only recognize those cases where participation of two or more firms in performing the audit of the financial statements could be an exception to the mandatory pre-issuance review if certain criteria are met, whether that arrangement is defined as a joint audit or not in the particular jurisdiction.
55. Regarding the fees generated at a group level, the IESBA agreed that firms should consider fees from related entities of the audit client in calculating the total fees from the client, in accordance with the related entity provision of the IIS (paragraph R400.20).<sup>18</sup>
56. Furthermore, the IESBA is proposing application material regarding the calculation of the total fees of the firm. (See paragraph 410.13 A2.) The IESBA recognizes that firms may not be able to determine an exact ratio regarding fee dependency. Accordingly, when the 15 percent threshold is

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<sup>15</sup> By inserting a new subsection on enhanced transparency of fee-related information of PIE audit clients in Section 410, the provisions on communication about fee dependency have now been moved to that subsection. (See paragraph R410.24.)

<sup>16</sup> In line with the Structure drafting guidelines for the Code, "firm" does not include network firms; therefore, it is permitted that the professional accountant who performs the review be a member of a network firm.

<sup>17</sup> Proposed ISQM 2, *Engagement Quality Reviews*

<sup>18</sup> The IESBA notes that this proposal is not intended to differ from the approach taken in the extant Code, even though the extant requirement (paragraph R410.4) includes an explicit reference to "fees from the audit client and its related entities."

exceeded and the firm has to disclose that information to TCWG and to the public, the proposals only require the disclosure of that fact and not of the exact ratio. (See paragraphs R410.24(a) and R410.25(c).)

#### Fee Dependency Continuing for an Extended Period

57. In line with the extant Code, in the case of fee dependency with respect to PIEs, the proposals do not require firms to apply a pre-issuance review but require a determination of whether such a pre-issuance review might be a safeguard to reduce the threats to an acceptable level. If the fee dependency continues beyond two years, the firm would be required to make the same determination every year. However, as the firm might determine that the application of a pre-issuance review is not an effective safeguard, application of the conceptual framework<sup>19</sup> might lead the firm to conclude that it should cease to be the auditor.
58. Even if a pre-issuance review continues to be a safeguard every year after the second year, the IESBA is of the view that fee dependency on an audit client that is a PIE cannot continue indefinitely. This is because after a certain period of time, the fee dependency would become so persistent and fundamental that no safeguards would be capable of reducing the threats to an acceptable level. Therefore, the IESBA is proposing that the Code should require the firm to cease to be the auditor if the fee dependency continues for more than five consecutive years. (See paragraph R410.19.) In determining this maximum time horizon, the IESBA took into account that recently adopted rules in Europe already specify a maximum five years in the case of fee dependency for PIE audit clients.<sup>20</sup>
59. In relation to this proposed requirement in paragraph R410.19, the IESBA noted that in some jurisdictions, laws or regulations might prohibit firms from resigning as auditor from a client relationship. The IESBA agreed that the Code already addresses such a circumstance in the overarching requirement in Section 100<sup>21</sup> to the effect that the Code cannot override laws and regulations. Therefore, if laws or regulations prohibit a firm from ending the audit engagement after five years, the firm must continue to be the auditor for such period as required under those laws or regulations.
60. The IESBA also heard from some stakeholders during its project outreach that there could be exceptional circumstances when it would be in the public interest that the firm does not cease to be the auditor for the client. Recognizing that those situations might arise, the IESBA agreed to propose an exception for firms to continue as auditor if there is a compelling reason with regard to the public interest, provided that certain criteria are met. (See paragraphs R410.20 and 410.20 A1.)
61. Specifically, to ensure that this allowance is used only on an exceptional basis, the IESBA is proposing that firms consult with and receive the concurrence of an independent regulatory body or professional body in the relevant jurisdiction. The IESBA is of the view that in the particular jurisdictions, these bodies have the necessary knowledge about the specificities of the market and, at the same time, should have the authority to create procedures for providing concurrence.
62. Some stakeholders have noted that the proposed requirement to cease the audit relationship after

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<sup>19</sup> Paragraph R120.10

<sup>20</sup> 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

<sup>21</sup> Paragraph R100.3 sets out the following: "A professional accountant shall comply with the Code. There might be circumstances where laws or regulations preclude an accountant from complying with certain parts of the Code. In such circumstances, those laws and regulations prevail, and the accountant shall comply with all other parts of the Code."

five years might raise issues with national anti-competition or anti-trust laws. To better understand the overall impact of such a requirement in the Code, the IESBA is seeking the views of professional bodies and regulators in particular about the operability of such a requirement within the framework of national laws and regulations.

*Fee Dependency in the Case of Audit Clients that Are Non-PIEs*

A Threshold for Re-evaluating Threats

63. The IESBA is proposing a similar model for addressing the threats for non-PIE audit clients as for the Code's existing fee dependency model for PIE audit clients but allowing greater latitude in the threshold and safeguards adopted. The IESBA considered this would be a reasonable approach bearing in mind the nature of the threats, the special considerations relating to small and medium practices (SMPs), the public interest, and the IESBA's new PIE project that will revisit the definition of a PIE.
64. Regarding a threshold, the fact-finding activities leading up to the Fees project provided no empirical evidence as to what it should be. Therefore, taking into account the considerations set out in the paragraph above and feedback from stakeholders, including the IFAC SMP Committee, the IESBA proposes that when total fees from an audit client that is not a PIE exceed 30% of the firm's total fee income for each of 5 consecutive years, the firm determine whether one of the following two actions might be a safeguard and, if so, apply it: (a) prior to issuing the audit opinion on the fifth year's financial statements, have a professional accountant, who is not a member of the firm, review the fifth year's audit work; or (b) after the audit opinion on the fifth year's financial statements has been issued and before issuance of the audit opinion on the sixth year's financial statements, have a professional accountant, who is not a member of the firm, or a professional body review the fifth year's audit work. Recognizing the need for proportionality, the IESBA is not proposing that in the case of non-PIEs, the pre-issuance review be equivalent to an engagement quality review. (See paragraph R410.14.)
65. The IESBA is proposing that firms make the same determination and take the same action should the fee dependency continue beyond the fifth year. In addition, as in the case of audit clients that are PIEs, the IESBA is proposing that when two or more firms are engaged to perform the audit, the involvement of the other firm may be regarded each year as an action equivalent to the pre-issuance review above provided that each firm performs sufficient work to take full responsibility for the audit opinion. However, this option is only relevant when the circumstances addressed by the proposed requirement on fee dependency apply to only one of the firms expressing the audit opinion. (See paragraphs R410.15 and R410.16.)
66. On balance, given that the extent of public interest in non-PIEs is lower than in PIEs, the IESBA agreed not to propose that firms be required to cease to be the auditor if fee dependency continues beyond five years in the case of audit clients that are non-PIEs.
67. During the development of the proposals, the IESBA heard views from some stakeholders that the proposed changes might create an unnecessary burden, especially for SMPs. The IESBA notes that inserting a threshold is not likely to change significantly the expectations as already set out in the Code. Based on the provisions of the extant Code, at such level of fee dependency firms most likely will reach the conclusion that the threats created are not at an acceptable level and would therefore be required to take certain actions. The aim of the proposal is to create a comprehensive and consistent approach regarding the expectations in the case of non-PIE audit clients as well, bearing



in mind that the conceptual framework and the general provisions applicable to all audit clients would still apply even in those cases when the specific threshold is not exceeded.

68. Also, unlike in the case of the proportion of fees for services other than audit to audit fees, fee dependency on an audit client is determined only at a firm level, not at a network level. Therefore, the IESBA does not believe that establishing a threshold will result in a complex evaluation process, given that the information necessary for the calculation of the total fees of the firm should be available within the firm.
69. Nevertheless, recognizing that the thresholds proposed are not scientifically determined, the IESBA will consider reviewing the thresholds after a period of implementation experience to assess whether any adjustments would be appropriate. Such assessment will also take into account the outcome of the PIE project.
70. The IESBA also considered whether to require communication with TCWG as a possible further action to mitigate the threats. However, taking into account feedback from stakeholders, including from its Consultative Advisory Group (CAG), the IESBA agreed that communication with TCWG would generally not be an effective tool to mitigate threats in the case of non-PIEs, given the less formal and less structured governance arrangements that commonly apply in that context.

#### **E. Transparency of Information Regarding Fees for Audit Clients that Are PIEs**

71. As highlighted in the Background and Overview section above, one of the main proposals in this Exposure Draft is enhanced transparency about fee-related information for PIE audit clients to TCWG and the public. The IESBA believes that such enhanced transparency can serve to better inform the views and decisions of TCWG and a wide range of stakeholders about the firm's independence. (See paragraph 410.3 A2.)

#### *Communication About Fee-related Information with Those Charged with Governance*

72. ISA 260 (Revised) requires that in the case of listed entities, auditors communicate with TCWG regarding "the 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. These fees shall be allocated to categories that are appropriate to assist TCWG in assessing the effect of services on the independence of the auditor."<sup>22</sup>
73. Regarding the role of TCWG, the Code encourages regular communication between the 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, applicable professional standards, laws or regulations. It adds that such communication enables TCWG to consider the firm's judgments and actions in identifying, evaluating and addressing threats, and to take appropriate action.<sup>23</sup>
74. Building on those provisions in ISA 260 (Revised) and the Code, the IESBA is proposing that in the case of PIEs, a firm be required to communicate not only the fees for audit and services other than audit, but also the firm's assessment of the level of the threats to independence created and any actions the firm has taken or proposes to take to reduce such threats to an acceptable level. Such communication would include the audit fees paid by the audit client to non network firms. (See paragraphs R410.22 and R410.23.) Additionally, as noted in paragraph 56 above, in the case of fee

<sup>22</sup> ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 17(a)(i)

<sup>23</sup> Paragraph 400.40 A2

dependency for PIE audit clients, the IESBA is proposing that the firm communicates that fact with TCWG, the actions taken to address the threats, and any proposal for the firm to continue as the auditor if the fee dependency continues beyond five consecutive years (see paragraph R410.24).

75. The main purpose of the proposed enhanced provisions with respect to communication with TCWG is to provide a basis for a meaningful, two-way discussion about fee-related matters to assist TCWG in assessing the firm's independence (see paragraph 410.21 A1). In this regard, the IESBA is proposing application material setting out examples of matters that the firm might consider communicating with TCWG to provide appropriate background and context about the audit engagement and services other than audit provided to the client, and the related fees. (See paragraph 410.23 A1.)
76. Regarding the communication about the level of the audit fee, the proposed application material in paragraph 410.22 A1 includes examples of considerations affecting the determination of the audit fee that the firm might consider discussing with TCWG. The IESBA expects that in most cases, firms would be able to inform TCWG that they are satisfied about the fees charged. If not, the IESBA expects that they would engage in an appropriate dialogue with TCWG about the actions taken or proposed.

#### Coordination with the IAASB

77. One of the issues the IESBA identified for coordination with the IAASB was that the pre-existing requirement in ISA 260 (Revised) on communication of independence matters, including fee-related information, is applicable only for listed entities whereas the IESBA's proposal covers PIEs. The IAASB considered various options to address this difference in scope. Given the accelerated timeline for the PIE project, however, the IAASB came to the view that it should defer further consideration of alignment in scope. The IAASB agreed that once all the relevant IESBA projects, i.e., the Fees, NAS and PIE projects, have been finalized, it can consider whether to add any application material to ISA 260 (Revised), broaden its scope or develop other consequential changes. In the meantime, the IAASB will monitor the progress of the IESBA projects.

#### *Public Disclosure of Fee-related Information*

78. The IESBA is proposing in paragraph R410.25 that for a PIE audit client, a firm be satisfied that the following information is publicly disclosed in a timely and accessible manner:
  - (a) The fee for the audit of the financial statements;
  - (b) Fees for services other than audit provided by the firm or a network firm (as discussed in paragraph 45 above); and
  - (c) If applicable, the fact of fee dependency (as flagged in paragraph 56 above).

This proposal is further discussed below.

#### Possible Ways to Effect Public Disclosure and Coordination with the IAASB

79. In proposing public disclosure of fee-related information, the IESBA intends that firms have flexibility to achieve such transparency.
80. First, the IESBA recognizes that several jurisdictions already have laws and regulations regarding public disclosure of fee-related information. Also, in certain circumstances, laws and regulations might prohibit public disclosure. In those instances, consistent with the overarching provision in

paragraph R100.3 of the Code, laws and regulations prevail. As it is not always possible to determine whether laws and regulations differ or go beyond the provisions of the Code regarding the extent of the information to be disclosed, to avoid duplication of obligations in relation to public disclosure, the proposal recognizes compliance with such laws and regulations as compliance with the Code if those national requirements substantively satisfy the requirement in the Code. (See paragraphs R410.25 and 410.25 A2.)

81. If there is no disclosure requirement in laws or regulations, the IESBA proposes guidance regarding how the disclosure requirement could be met. Since it is not within the IESBA's remit to establish disclosure requirements for audit clients, the proposed requirement is expressed as an obligation of the firm. However the IESBA would anticipate that the firm would have the opportunity to consult with the client as to whether the client might agree to disclose the information, for example in the financial statements, the annual report or in the proxy statement. If necessary though, the firm has the responsibility to make such disclosure in a manner deemed appropriate in the circumstances, taking into account the important condition of appropriate accessibility (i.e., the information is readily available for any stakeholder in a manner that stakeholders are specifically informed about or the firm has reason to believe that stakeholders know about). (See paragraphs 410.25 A3 and 410.25 A6.)
82. An example of suitable location of such disclosure by the firm is the audit report. In this regard, following coordination with and input from the IAASB, the IESBA is proposing guidance explaining which part of the audit report would be the appropriate place for such disclosure (see paragraph 410.25 A4).

#### Fee-related Information to be Disclosed

83. In deliberating the proposal for public disclosure of fee-related information, the IESBA noted concerns that disclosing unsolicited information to the public without providing comparable information (such as fee-related information from previous financial years) or further explanation might be misleading.
84. The IESBA's objective with this proposal is to achieve transparency for the benefit of stakeholders in facilitating their judgments and assessments about a firm's independence. It is not the IESBA's intent in the proposal to achieve comparability of fee information across different entities and groups. Accordingly, the IESBA believes that it should be left to firms to determine how best to fulfill the transparency objective and that the Code should not be prescriptive in that regard. However, to assist firms determine the matters that might be relevant for the communication, the IESBA is proposing guidance setting out examples of information that firms might consider providing as part of such disclosure. (See paragraph 410.25 A5.)
85. For clarity, the IESBA is proposing guidance explaining that the fees to be disclosed are those that usually reflect the fees paid or estimated to be paid for the services based on the information available at the time of the disclosure. (See paragraph 410.25 A1.)
86. Concerning the level of the audit fee in the case of a group audit, the IESBA intends for stakeholders to have information about the full cost of the group audit, being fees for audit work performed on the engagement by the firm and network firms, and by firms outside the network. The IESBA believes that this information would assist stakeholders in making judgments about the independence of all those involved in the group audit and not only the firm or network firms. However, recognizing that fee information from component auditors outside the firm's network might not be readily available, the proposal specifies that in relation to those component auditors, the fee information to be disclosed

is the actual or estimated fees paid or payable to them. (See paragraph R410.25 (a).)

87. The IESBA also understands that there might be circumstances where the firm is simply not able to obtain information necessary from a component auditor outside the firm's network in order to effect the disclosure. Accordingly, the IESBA is proposing an exception to the disclosure requirement in those circumstances. In such a case, the firm would be required to be satisfied that the fee information that is available is publicly disclosed together with an explanation, to the extent possible, of the qualitative significance of the fee information which is not available. (See paragraph R410.26.)
88. During its coordination discussions with the IAASB<sup>24</sup> as well as its own deliberations in developing this specific proposal regarding public disclosure of the fee for the audit of group financial statements, the IESBA noted various concerns about the practicality of the proposal and the burden it would place on firms to collate the information. The IESBA considers that the overriding public interest in transparency to inform the judgments and assessments of stakeholders about the independence of those involved in the group audit outweighs those concerns. Nevertheless, the IESBA would welcome views from stakeholders on this proposed requirement, including whether they support it or have specific concerns about its operability.

#### **F. Operability of the Proposals in the Context of Anti-trust Laws**

89. During the course of the project, the IESBA heard concerns, including among some within the IESBA CAG and the [Forum of Firms](#), that the proposals could raise potential issues with regard to anti-trust laws in some jurisdictions. For example, the IESBA understands that in certain jurisdictions, anti-trust laws could preclude the promulgation of independence provisions that are deemed to impact competitive practices (whether in relation to pricing activities or otherwise) if the national standard setter is a private body. The IESBA also understands that this preclusion would apply even if the provisions were considered to promote the public interest, unless they enhance competition. Nevertheless, the IESBA understands that regulatory bodies in such jurisdictions are generally less restricted in their ability to set rules in the public interest and may therefore be open to considering adopting provisions promulgated by the IESBA if they have the authority to set independence requirements.
90. To further understand the interaction of the proposals with national anti-trust laws, the IESBA will consult further on the matter but would welcome the views of stakeholders as to whether the proposals could be adopted by national standard setters or IFAC member bodies (whether or not they have a regulatory remit).

#### **G. Other Revisions to Part 4A**

91. The IESBA is also proposing:
- With respect to overdue fees, clarification as to the nature of fees and the period of reference the firm should consider when evaluating the level of self-interest threat created (see paragraphs 410.11 A1 and 410.11 A2).
  - Enhanced guidance on factors relevant to evaluating the level of self-interest threat created by overdue fees (see paragraph 410.11 A3).

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<sup>24</sup> The IAASB is currently undertaking a project to revise ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*. The IESBA will continue its coordination with the IAASB on the Fees project in the context of the IAASB's revision of ISA 600.

- Enhanced guidance on actions that might be safeguards in relation to fee dependency at the firm, office and partner levels (see paragraphs 410.13 A4 and 410.13 A7).
- Through a consequential amendment to Section 270,<sup>25</sup> enhanced guidance regarding undue pressure exerted by a professional accountant (who, for example, might be a member of management or TCWG) on another accountant in relation to the level of the fee for a professional service. (See paragraph 270.3 A3.)
- Through a consequential amendment to Section 320,<sup>26</sup> enhanced guidance regarding the level of fees relative to the resources required as a factor to take into account when considering whether to accept an engagement. (See paragraph 320.3 A4.)

#### H. Matters Relevant to Section 905

92. The IESBA also considered whether the changes proposed to Part 4A have implications for assurance engagements other than audit and review engagements (referred to as assurance engagements). The IESBA was mindful of the special considerations for those engagements, particularly that parties involved in an assurance engagement might not be the same and therefore the application of the independence provisions in Part 4B might vary.<sup>27</sup>
93. The IESBA is of the view that, as in the case of audit engagements, there is an inherent self-interest threat when fees for an assurance engagement are negotiated with and paid by the assurance client. The IESBA recognizes that by the nature of assurance engagements, many of which might be limited in scope, for a narrow purpose and non-recurring, firms more likely will reach the conclusion that the threats created are at an acceptable level. Nevertheless, the IESBA is proposing that the Code also explicitly articulate the existence of such threats even in the case of assurance engagements. (See paragraph 905.3 A1.)
94. On balance, the IESBA believes that the threats created by fees for services other than the assurance engagement are not generally such that they require formal evaluation, other than where (as in the extant Code) the total fees derived from the assurance client are significant. However, the IESBA believes it is appropriate for the Code to make clear that the threats created by significant fee dependency do require evaluation even if the assurance client is not in fact the one paying for the assurance engagement. (See paragraph 905.10 A2.)
95. In relation to overdue fees in Section 905, the proposals do not include a general expectation that the firm obtain payment of overdue fees before the assurance report is issued. Such an expectation is included in extant paragraph 905.4 A1, albeit only in relation to overdue fees for a prior period assurance engagement. The IESBA would welcome stakeholders' views as to whether, following the consequential amendments for assurance engagements to consider all overdue fees, it would be appropriate to include a general expectation regarding payment as proposed for audit engagements in paragraph 410.11. A2.
96. The IESBA does not consider it necessary to include in Part 4B similar requirements and application material in Part 4A that are relevant only for PIE clients.

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<sup>25</sup> Section 270, *Pressure to Breach the Fundamental Principles*

<sup>26</sup> Section 320, *Professional Appointments*

<sup>27</sup> Paragraph 900.11 A2 in the [revised Part 4B](#), issued by the IESBA in January 2020

**IV. Analysis of Overall Impact of the Proposed Changes**

- 97. The IESBA believes that the proposals represent a significant strengthening of the extant fee-related provisions of the IIS and that they will help address public perceptions about auditor independence in relation to fees, especially vis-à-vis audit clients. The public interest will be served by having a Code that contains robust and high-quality provisions that enable consistent application by firms in differing legal frameworks across jurisdictions, thereby increasing confidence in the independence of firms.
- 98. The changes have implications for national standard setters and IFAC member bodies that have adopted the Code or use it as a basis or a benchmark for their own ethics standards.
- 99. The IESBA does not intend the proposals to impact or otherwise influence the level of fees or the fee arrangements for any services provided by firms. However, in certain cases mainly for audit clients, the actions firms may take to address the threats to independence created by the fees paid by the clients for audit and services other than audit could result in additional costs. The nature and significance of those costs will depend on the particular circumstances.
- 100. Further, given the nature and extent of the proposed revisions to the Code in case of PIE audit clients, the IESBA believes that some of the proposals would entail significant changes to the policies and procedures for firms. Such changes may result in increased costs. In addition, in relation to the proposals regarding disclosure of fee-related matters with TCWG and to the public, the implementation of the provisions may lead to a greater commitment of time on the part of TCWG and management of audit clients in engaging with firms.
- 101. As with any changes to the Code, firms can expect implementation costs associated with awareness and training initiatives, translation where needed, and maintenance costs in updating their internal policies and methodologies.

**V. Project Timetable and Effective Date**

- 102. The IESBA is mindful of the need for appropriate alignment in the finalization of the Fees and NAS pronouncements. It will also coordinate the effective dates for the final provisions from these projects with the effective date of the final provisions from the PIE project. Information about IESBA's projects and its timetable is available at: [www.ethicsboard.org/consultations-projects](http://www.ethicsboard.org/consultations-projects).
- 103. The indicative timeline for the Fees Project is set out below.

June 2020	Highlights of significant comments on the Exposure Draft to the IESBA
September 2020	<ul style="list-style-type: none"> <li>• Discussion of significant issues arising on exposure with the IESBA CAG</li> <li>• Full IESBA review of respondents' comments and first read of revised proposals</li> </ul>
December 2020	IESBA approval of final pronouncement

**VI. Guide for Respondents**

- 104. The IESBA welcomes comments on all matters addressed in this Exposure Draft, but especially those identified in the Request for Specific Comments below. Comments are most helpful when they refer

to specific paragraphs, include the reasons for the comments, and, where appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this Exposure Draft, it will be helpful for the IESBA to be made aware of this view.

### **Request for Specific Comments**

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

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)?
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?
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?

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

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?

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

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?

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

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?
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?

#### *Fee Dependency for PIE Audit Clients*

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?

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

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

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?
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?

*Anti-Trust and Anti-Competition Issues*

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.

*Proposed Consequential and Conforming Amendments*

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?
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?

**Request for General Comments**

105. In addition to the request for specific comments above, the IESBA is also seeking comments on the matters set out below:
  - *Those Charged with Governance, including Audit Committee Members* – The IESBA invites comments regarding any aspect of the proposals from individuals with responsibilities for governance and financial reporting oversight. This includes small businesses where a single owner manages the entity and also has a governance role.
  - *Small- and Medium-Sized Entities (SMEs) and Small and Medium Practices (SMPs)* – The IESBA invites comments regarding any aspect of the proposals from SMEs and SMPs.
  - *Regulators and Audit Oversight Bodies* – The IESBA invites comments on the proposals from an enforcement perspective from members of the regulatory and audit oversight communities.



## EXPLANATORY MEMORANDUM

- *Developing Nations* – Recognizing that many developing nations have adopted or are in the process of adopting the Code, the IESBA invites respondents from these nations to comment on the proposals, and in particular on any foreseeable difficulties in applying them in their environment.
- *Translations* – Recognizing that many respondents may intend to translate the final changes for adoption in their own environments, the IESBA welcomes comment on potential translation issues respondents may note in reviewing the proposals.

**EXPOSURE DRAFT: PROPOSED REVISIONS TO THE FEE-RELATED  
PROVISIONS OF THE CODE  
(CLEAN)**

**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 Section 330 sets out application material relevant to applying the conceptual framework where the level and nature of fees and other remuneration arrangements might create a self-interest threat to compliance with one or more of the fundamental principles. This section sets out specific requirements and application material relevant to applying the conceptual framework to identify, evaluate and address threats to independence arising from fees charged to audit clients.

**Requirements and Application Material**

**General**

- 410.3 A1 Fees for professional services are usually negotiated with and paid by the client and might create threats to independence. This practice is generally recognized and accepted by intended users of financial statements.
- 410.3 A2 When the audit client is a public interest entity, stakeholders have heightened expectations regarding the firm's independence. As transparency can serve to better inform the views and decisions of those charged with governance and a wide range of stakeholders, this section provides for disclosure of fee-related information to both those charged with governance and stakeholders more generally for audit clients that are public interest entities.
- 410.3 A3 For the purposes of this section, audit fees comprise fees or other types of remuneration for an audit or review of financial statements. Where reference is made to the fee for the audit of the financial statements, this does not include any fee for an audit of special purpose financial statements or a review of financial statements. (Ref: paragraphs R410.22(a), 410.22 A1, R410.25(a), 410.25 A1 and R410.26)

*Identifying and Evaluating Threats*

- R410.4** Before a firm or network firm accepts an audit or any other engagement for an audit client, the firm shall determine whether the threats to independence created by the fees proposed to the client are at an acceptable level. The firm shall also re-evaluate such threats where appropriate during the engagement period for the audit if circumstances change.
- 410.4 A1 When fees are negotiated with and paid by the audit client, this creates a self-interest threat and might create an intimidation threat to independence.

- 410.4 A2 Factors that are relevant in evaluating the level of threats created when fees for an audit or any other engagement are paid by the audit client include:
- Whether there is external review of the quality of the firm's audit work.
  - The level of the fees and the extent to which they have regard to the resources required, taking into account the firm's commercial and market priorities and position.
  - The involvement of those charged with governance in appointing the auditor and agreeing fees, and the apparent emphasis they and client management place on the quality of the audit and the overall level of the fees.
  - Any linkage between fees for the audit and those for services other than audit, and the relative size of both elements.
  - The extent of any dependency between the level of the fee for, and the outcome of, the service.
  - The significance of the client, for example to the firm, network, partner or office.
  - The nature of the client, for example whether the client is a public interest entity.
- 410.4 A3 The conditions, policies and procedures described in paragraph 120.12 A3 (particularly the existence of a quality management system designed and implemented by the firm in accordance with [proposed] ISQM 1) might also impact the evaluation of whether the threats to independence are at an acceptable level.
- 410.4 A4 The requirements and application material that follow identify circumstances which might need to be further evaluated when determining whether the threats are at an acceptable level. For those circumstances, application material includes examples of additional factors that might be relevant in evaluating the threats.

### **Level of Audit Fees**

- 410.5 A1 Determining the fees to be charged to an audit client, whether for audit or other services, is a business decision of the firm taking into account the facts and circumstances relevant to that specific engagement, including the requirements of technical and professional standards.
- 410.5 A2 In addition to the factors identified in paragraph 410.4 A2, factors that are relevant in evaluating self-interest and intimidation threats created by the level of the audit fee paid by the audit client include:
- The firm's commercial rationale for the audit fee.
  - Whether pressure has been or is being applied by the client to reduce the audit fee.
- 410.5 A3 Examples of actions that might be safeguards to address such threats include:
- Having an appropriate reviewer who was not involved in the audit engagement assess the reasonableness of the fee proposed having regard to the scope and complexity of the engagement.
  - Having an appropriate reviewer who was not involved in the audit engagement review the work undertaken.

*Impact of Other Services Provided to an Audit Client*

- R410.6** A firm shall not allow 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.
- 410.6 A1 The audit fee ordinarily reflects a combination of matters, such as those identified in paragraph 410.22 A1. However, the provision of other services to the audit client is not an appropriate consideration in determining the audit fee.
- 410.6 A2 Paragraph R410.6 is not intended to prohibit cost savings that can be achieved as a result of experience derived from the provision of services other than audit to the audit client.

**Contingent Fees**

- 410.7 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 charged through an intermediary is an example of an indirect contingent fee. In this section, a fee is not regarded as being contingent if established by a court or other public authority.
- R410.8** A firm shall not charge directly or indirectly a contingent fee for an audit engagement.
- R410.9** A firm or network firm shall not charge directly or indirectly a contingent fee for a non-assurance service provided to an audit client, if:
- (a) The fee is charged by the firm expressing the opinion on the financial statements and the fee is material or expected to be material to that firm;
  - (b) The fee is charged by a network firm that participates in a significant part of the audit and the fee is material or expected to be material to that firm; or
  - (c) The outcome of the non-assurance service, and therefore the amount of the fee, is dependent on a future or contemporary judgment related to the audit of a material amount in the financial statements.
- 410.9 A1 Paragraphs R410.8 and R410.9 preclude a firm or a network firm from entering into certain contingent fee arrangements with an audit client. Even if a contingent fee arrangement is not precluded when providing a non-assurance service to an audit client, it might still impact the evaluation of the level of the self-interest threat.
- 410.9 A2 Factors that are relevant in evaluating the level of such a threat include:
- The range of possible fee amounts.
  - Whether an appropriate authority determines the outcome on which the contingent fee depends.
  - Disclosure to intended users of the work performed by the firm and the basis of remuneration.
  - The nature of the service.
  - The effect of the event or transaction on the financial statements.
- 410.9 A3 Examples of actions that might be safeguards to address such a self-interest threat include:
- Having an appropriate reviewer who was not involved in performing the non-assurance service review the work performed by the firm.

- Obtaining an advance written agreement with the client on the basis of remuneration.

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

410.10 A1 The evaluation of the level of the self-interest threat might be impacted when a large proportion of fees charged by the firm or network firms to an audit client is generated by providing services other than audit to the client, due to concerns about the potential loss of either the audit engagement or other services. Such circumstances might also create an intimidation threat. A further consideration is a perception that the firm or network firm focuses on the non-audit relationship, which might create a threat to the auditor's objectivity.

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

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

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

#### **Total Fees – Overdue Fees**

410.11 A1 The evaluation of the level of the self-interest threat might be impacted if fees payable by the audit client for the audit or services other than audit are overdue during the period of the audit engagement.

410.11 A2 It is generally expected that the firm will obtain payment of such fees before the audit report is issued.

410.11 A3 Factors that are relevant in evaluating the level of such a self-interest threat include:

- The significance of the overdue fees to the firm.
- The length of time the fees have been overdue.
- The firm's assessment of the ability and willingness of the client to pay the overdue fees.

410.11 A4 Examples of actions that might be safeguards to address such a self-interest threat include:

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

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

- (a) Whether the overdue fees might be equivalent to a loan to the client in which case the requirements and application material set out in section 511 are applicable; and

- (b) Whether it is appropriate for the firm to be re-appointed or continue the audit engagement.

### **Total Fees – Fee Dependency**

#### *All Audit Clients*

- 410.13 A1 When the total fees generated from an audit client by the firm expressing the audit opinion represent a large proportion of the total fees of that firm, the dependence on, and concern about the potential loss of fees from audit and other services from that client impact the evaluation of the level of the self-interest threat and create an intimidation threat.
- 410.13 A2 In calculating the total fees of the firm, the firm might use financial information available from the previous financial year and estimate the proportion based on that information if appropriate.
- 410.13 A3 Factors that are relevant in evaluating the level of such threats include:
- The operating structure of the firm.
  - The qualitative and quantitative significance of the audit client to the firm.
  - Whether the firm is expected to expand such that the significance of the client is likely to reduce.
- 410.13 A4 Examples of actions that might be safeguards to address such self-interest and intimidation threats include:
- Having an appropriate reviewer who is not a member of the firm review the audit work.
  - Reducing the extent of services other than audit provided to the audit client.
  - Increasing the client base of the firm to reduce dependence on the client.
  - Increasing the extent of services provided to other clients.
- 410.13 A5 A self-interest or intimidation threat is created when the fees generated by a firm from an audit client represent a large proportion of the revenue of one partner or one office of the firm.
- 410.13 A6 Factors that are relevant in evaluating the level of such threats include:
- The qualitative and quantitative significance of the audit client to the partner or office.
  - The extent to which the compensation of the partner, or the partners in the office, is dependent upon the fees generated from the client.
- 410.13 A7 Examples of actions that might be safeguards to address such self-interest and intimidation threats include:
- Having an appropriate reviewer who was not involved in the audit engagement review the audit work.
  - Ensuring that the compensation of the partner is not significantly influenced by the fees generated from the client.
  - Reducing the extent of services other than audit provided by the partner or office to the audit client.
  - Increasing the client base of the partner or the office to reduce dependence on the client.
  - Increasing the extent of services provided by the partner or the office to other clients.

## Audit Clients that are Not Public Interest Entities

- R410.14** When for each of five consecutive years total fees from an audit client that is not a public interest entity represent, or are likely to represent, more than 30% of the total fees received by the firm, the firm shall determine whether either of the following actions might be a safeguard to reduce the threats created to an acceptable level, and if so, apply it:
- (a) Prior to the audit opinion being issued on the fifth year's financial statements, have a professional accountant, who is not a member of the firm expressing the opinion on the financial statements review the fifth year's audit work; or
  - (b) After the audit opinion on the fifth year's financial statements has been issued, and before the audit opinion is issued on the sixth year's financial statements, have a professional accountant, who is not a member of the firm expressing the opinion on the financial statements or a professional body review the fifth year's audit work.
- R410.15** If the total fees described in paragraph R410.14 continue to exceed 30%, the firm shall each year determine whether either of the actions in paragraph R410.14 applied to the relevant year's engagement might be a safeguard to address the threats created by the total fees received by the firm from the client, and if so, apply it.
- R410.16** When two or more firms are engaged to conduct an audit of the client's financial statements, the involvement of the other firm in the audit may be regarded each year as an action equivalent to that in paragraph R410.14 (a), if:
- (a) The circumstances addressed by paragraph R410.14 apply to only one of the firms expressing the audit opinion; and
  - (b) Each firm performs sufficient work to take full individual responsibility for the audit opinion.

## Audit Clients that are Public Interest Entities

- R410.17** When for each of two consecutive years the total fees from an audit client that is a public interest entity represent, or are likely to represent, more than 15% of the total fees received by the firm, the firm shall determine whether, prior to the audit opinion being issued on the second year's financial statements, an engagement quality review performed by a professional accountant who is not a member of the firm expressing the opinion on the financial statements ("pre-issuance review") might be a safeguard to reduce the threats to an acceptable level, and if so, apply it.
- R410.18** When two or more firms are engaged to conduct an audit of the client's financial statements, the involvement of the other firm in the audit may be regarded each year as an action equivalent to that in paragraph R410.17, if:
- (a) The circumstances addressed by paragraph R410.17 apply to only one of the firms expressing the audit opinion; and
  - (b) Each firm performs sufficient work to take full individual responsibility for the audit opinion.
- R410.19** Subject to paragraph R410.20, if the circumstances described in paragraph R410.17 continue for five consecutive years, the firm shall cease to be the auditor after the audit opinion for the fifth year is issued.

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

- (a) The firm consults with an independent regulatory body or professional body in the relevant jurisdiction and it concurs that having the firm continue as the auditor would be in the public interest; and
- (b) Before the audit opinion on the sixth and any subsequent year's financial statements is issued, the firm engages a professional accountant who is not a member of the firm expressing the opinion on the financial statements to perform a pre-issuance review.

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

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

#### *Communication About Fee-related Information with Those Charged with Governance*

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

#### Audit Fees

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

- (a) The level of the fee for the audit of the financial statements on which the firm issued an opinion;
- (b) Any fees for the audit of special purpose financial statements and review engagements; and
- (c) Whether the threats created by the level of the audit fees are at an acceptable level and any actions the firm has taken or proposes to take to reduce such threats to an acceptable level.

410.22 A1 The objective of such communication is to provide the background and context to the audit fee to enable those charged with governance to consider the independence of the firm. The nature and extent of matters to be communicated will depend on the facts and circumstances and might include for example:

- Considerations affecting the level of the fee such as:
  - The scale, complexity and geographic spread of the audit client's operations.
  - The time spent or expected to be spent commensurate with the scope and complexity of the audit.
  - The cost of other resources utilized or expended in performing the audit.



- The quality of record keeping and processes for financial statements preparation.
- Adjustments to the fee quoted or charged during the period of the audit, and the reasons for any such adjustments.
- Changes to laws and regulations and professional standards relevant to the audit that impacted the fee.

410.22 A2 The firm is encouraged to provide such information as soon as practicable and communicate proposed adjustments as appropriate.

#### Fees for Services Other than Audit

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

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

410.23 A1 The objective of such communication is to provide the background and context to the fees for services other than audit to enable those charged with governance to consider the independence of the firm. The nature and extent of matters to be communicated will depend on the facts and circumstances and might include for example:

- The amount of fees from services other than audit that are required by laws and regulations.
- The nature of other services provided and their associated fees.
- Information on the nature of the services provided under a general policy approved by those charged with governance and associated fees.
- The proportion of fees referred to in paragraph R410.23(a) to the aggregate of the audit fees charged by the firm and network firms.

#### Fee Dependency

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

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

- (c) Any proposal to continue as the auditor under paragraph R410.20.

*Public Disclosure of Fee-related Information*

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

- (a) Subject to paragraph R410.26, the fee for the audit of the financial statements on which the firm issued an opinion, comprising
- (i) Fees paid or payable to the firm and network firms, and
  - (ii) Actual or estimated fees paid or payable to other firms that have performed audit procedures on the engagement;
- (b) The total amount of fees charged during the period covered by the financial statements for the provision of services by the firm or a network firm to the audit client, which, for this purpose shall include only related entities over which the client has direct or indirect control, other than as disclosed under (a); and
- (c) If applicable, the fact that the total fees received by the firm from the audit client represent, or are likely to represent, more than 15% of the total fees received by the firm for two consecutive years, and the year that this situation first arose.

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

410.25 A1 The fees disclosed usually reflect the fees paid or estimated to be paid for the services based on the information available at the time of the disclosure. The fees paid or estimated to be paid for the audit engagement include all such fees paid or payable to firms in relation to the audit work performed on which the audit opinion is based.

410.25 A2 An example of when compliance with laws and regulations would not substantively satisfy paragraph R410.25 is in the case of disclosure of fees for services other than audit, the exclusion of fees for services provided by network firms to the audit client and related entities over which the client has direct or indirect control.

410.25 A3 Such information might be disclosed,

- (a) By the audit client in its financial statements, annual report or proxy statement, or
- (b) If not by the audit client, by the firm in a manner deemed appropriate for the circumstances .

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

410.25 A5 The firm might also discuss with the client whether disclosure of other information relating to fees might enhance the users' understanding of the fees paid or payable and how they might influence the firm's independence. The nature and extent of matters to be considered will depend on the facts and circumstances and might include for example:

- Comparative information for the prior year's fees for audit and services other than audit.
- The nature of services and their associated fees as disclosed under paragraph

R410.25(b).

- Safeguards applied when the total fees from the client represent or are likely to represent 15% of the total fees received by the firm.

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

**R410.26** As an exception to paragraph R410.25(a), where the audit client does not make the disclosure specified in R410.25(a) and the firm is not able to obtain or provide an estimate of the fees referred to in paragraph R410.25(a)(ii), the firm shall be satisfied that the fee information that is available is publicly disclosed together with an explanation, to the extent possible, of the qualitative significance of the fee information which is not available.

*Considerations for Review Clients*

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

## PART 4B – INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

### SECTION 905

#### FEES

##### Introduction

- 905.1 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.
- 905.2 Fees or other types of remuneration might create a self-interest or intimidation threat. This section sets out specific requirements and application material relevant to applying the conceptual framework to identify, evaluate and address threats to independence arising from fees charged to assurance clients.

##### Requirements and Application Material

###### *Identifying and Evaluating Threats*

- R905.3** Before a firm accepts an assurance engagement, the firm shall determine whether the threats to independence created by the fees proposed to the assurance client are at an acceptable level. The firm shall also re-evaluate such threats where appropriate during the engagement period if circumstances change.
- 905.3 A1 When fees are negotiated with and paid by the assurance client, this creates a self-interest threat and might create an intimidation threat to independence.
- 905.3 A2 Factors that are relevant in evaluating the level of threats created when fees are paid by the assurance client include:
- The nature of the assurance engagement.
  - Whether there is external review of the firm's system of quality management.
  - The level of the fees for the assurance engagement and the extent to which they have regard to the resources required, taking into account the firm's commercial and market priorities and position.
  - The extent of any dependency between the level of the fee for, and the outcome of, the service.
  - The significance of the client, for example to the firm or partner.
  - The nature of the client.
- 905.3 A3 The conditions, policies and procedures described in paragraphs 120.12 A3 (particularly the existence of a quality management system designed and implemented by a firm in accordance with [proposed] ISQM 1) might also impact the evaluation of whether the threats to independence are at an acceptable level.
- 905.3 A4 The requirements and application material that follow identify circumstances which might need to be further evaluated when determining whether the threats are at an acceptable level. For those circumstances, application material includes examples of additional factors that might be

relevant in evaluating the threats.

### **Level of Fees for Assurance Engagements**

- 905.4 A1 Determining the fees to be charged to an assurance client, whether for assurance or other services, is a business decision of the firm taking into account the facts and circumstances relevant to that specific engagement, including the requirements of technical and professional standards.
- 905.4 A2 In addition to factors identified in paragraph 905.3 A2, factors that are relevant in evaluating self-interest and intimidation threats created by the level of the fee for an assurance engagement when paid by the assurance client include:
- The firm's commercial rationale for the fee for the assurance engagement.
  - Whether pressure has been or is being applied by the client to reduce the fee for the assurance engagement.
- 905.4 A3 Examples of actions that might be safeguards to address such threats include:
- Having an appropriate reviewer who was not involved in the assurance engagement assess the reasonableness of the fee proposed having regard to the scope and complexity of the engagement.
  - Having an appropriate reviewer who was not involved in the assurance engagement review the work.

### **Contingent Fees**

- 905.5 A1 Contingent fees are fees calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed. A contingent fee charged through an intermediary is an example of an indirect contingent fee. In this section, a fee is not regarded as being contingent if established by a court or other public authority.
- R905.6** A firm shall not charge directly or indirectly a contingent fee for an assurance engagement.
- R905.7** A firm shall not charge directly or indirectly a contingent fee for a non-assurance service provided to an assurance client if the outcome of the non-assurance service, and therefore, the amount of the fee, is dependent on a future or contemporary judgment related to a matter that is material to the subject matter information of the assurance engagement.
- 905.7 A1 Paragraphs R905.6 and R905.7 preclude a firm from entering into certain contingent fee arrangements with an assurance client. Even if a contingent fee arrangement is not precluded when providing a non-assurance service to an assurance client, it might still impact the evaluation of the level of the self-interest threat.
- 905.7 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 subject matter information.

905.7 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 relevant assurance work.
- Obtaining an advance written agreement with the client on the basis of remuneration.

#### **Total Fees—Overdue Fees**

905.8 A1 The evaluation of the level of the self-interest threat might be impacted if fees payable by the assurance client for the assurance engagement or other services are overdue during the period of the assurance engagement.

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

- The significance of the overdue fees to the firm.
- The length of time the fees have been overdue.
- The firm's assessment of the ability and willingness of the client or other relevant party to pay the overdue fee.

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

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

**R905.9** When a significant part of fees due from an assurance 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 in which case the requirements and application material set out in Section 911 are applicable; and
- (b) Whether it is appropriate for the firm to be re-appointed or continue the assurance engagement.

#### **Total Fees—Fee Dependency**

905.10 A1 When the total fees generated from an assurance client by the firm expressing the conclusion in an assurance engagement represent a large proportion of the total fees of that firm, the dependence on, and concern about the potential loss of fees from that client impact the evaluation of the level of the self-interest threat and create an intimidation threat.

905.10 A2 A self-interest and intimidation threat is created in the circumstances described in paragraph 905.10 A1 even if the assurance client is not responsible for negotiating or paying the fees for the assurance engagement.

905.10 A3 In calculating the total fees of the firm, the firm might use financial information available from the previous financial year and estimate the proportion based on that information if appropriate.

905.10 A4 Factors that are relevant in evaluating the level of such threats include:

- The operating structure of the firm.

- The qualitative and quantitative significance of the assurance client to the firm.
- Where the firm is expected to expand such that the significance of the client is likely to reduce.

905.10 A5 Examples of actions that might be safeguards to address such self-interest and intimidation threats include:

- Reducing the extent of services other than assurance engagements provided to the client.
- Increasing the client base in the firm to reduce dependence on the assurance client.

905.10 A6 A self-interest or intimidation threat is also created when the fees generated by the firm from an assurance client represent a large proportion of the revenue from an individual partner's clients.

905.10 A7 Factors that are relevant in evaluating the level of such threats include:

- The qualitative and quantitative significance of the assurance client to the partner.
- The extent to which the compensation of the partner is dependent upon the fees generated from the client.

905.10 A8 Examples of actions that might be safeguards to address such a self-interest or intimidation threat include:

- Having an appropriate reviewer who was not an assurance team member review the work.
- Ensuring that the compensation of the partner is not significantly influenced by the fees generated from the assurance client.
- Increasing the client base of the partner to reduce dependence on the client.

## PROPOSED CONSEQUENTIAL AND CONFORMING AMENDMENTS

### (PROPOSED CHANGES SHADED IN GRAY)

#### SECTION 120

#### THE CONCEPTUAL FRAMEWORK

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#### Considerations for Audits, Reviews and Other Assurance Engagements

##### *Independence*

120.12 A1 Professional accountants in public practice are required by International Independence Standards to be independent when performing audits, reviews, or other assurance engagements. Independence is linked to the fundamental principles of objectivity and integrity. It comprises:

- (a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.
- (b) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude that a firm’s or an audit or assurance team member’s integrity, objectivity or professional skepticism has been compromised.

120.12 A2 International Independence Standards set out requirements and application material on how to apply the conceptual framework to maintain independence when performing audits, reviews or other assurance engagements. Professional accountants and firms are required to comply with these standards in order to be independent when conducting such engagements. The conceptual framework to identify, evaluate and address threats to compliance with the fundamental principles applies in the same way to compliance with independence requirements. The categories of threats to compliance with the fundamental principles described in paragraph 120.6 A3 are also the categories of threats to compliance with independence requirements.

120.12 A3 Conditions, policies and procedures described in paragraphs 120.6 A1 and 120.8 A2 that might assist in identifying and evaluating threats to compliance with the fundamental principles might also be factors relevant to identifying and evaluating threats to independence. In the context of audits, reviews and other assurance engagements the existence of a quality management system designed and implemented by a firm in accordance with [proposed] ISQM 1 is an example of such conditions, policies and procedures.



## 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 does not allow for sufficient and appropriate resources (including human, technological and intellectual property resources) to perform the services in accordance with technical and professional standards.

270.3 A4 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 330**

### **FEES AND OTHER TYPE OF REMUNERATION**

...

#### **Application Material**

##### **Level of Fees**

- 330.3 A1 The level of fees might impact a professional accountant's ability to perform professional services in accordance with technical and 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 determined and which professional services are covered.
  - (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:
- (a) Adjusting the level of fees or the scope of the engagement.
  - (b) Having an appropriate reviewer review the work performed.

## **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.
- The level of fees and the extent to which they have regard to the resources required, taking into account the professional accountant's commercial and market priorities and position.

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 ....

**EXPOSURE DRAFT: PROPOSED REVISIONS TO THE FEE-RELATED  
PROVISIONS OF THE CODE  
(MARK-UP FROM EXTANT CODE)**

**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 Section 330 sets out application material relevant to applying the conceptual framework where the level and nature of fees and other remuneration arrangements might create a self-interest threat to compliance with one or more of the fundamental principles. ~~The nature and level of fees or other types of remuneration might create a self-interest or intimidation threat.~~ This section sets out specific requirements and application material relevant to applying the conceptual framework to identify, evaluate and address threats to independence arising from fees charged to audit clients in such circumstances.

**Requirements and Application Material**

**General**

- 410.3 A1 Fees for professional services are usually negotiated with and paid by the client and might create threats to independence. This practice is generally recognized and accepted by intended users of financial statements.
- 410.3 A2 When the audit client is a public interest entity, stakeholders have heightened expectations regarding the firm's independence. As transparency can serve to better inform the views and decisions of those charged with governance and a wide range of stakeholders, this section provides for disclosure of fee-related information to both those charged with governance and stakeholders more generally for audit clients that are public interest entities.
- 410.3 A3 For the purposes of this section, audit fees comprise fees or other types of remuneration for an audit or review of financial statements. Where reference is made to the fee for the audit of the financial statements, this does not include any fee for an audit of special purpose financial statements or a review of financial statements. (Ref: paragraphs R410.22(a), 410.22 A1, R410.25(a), 410.25 A1 and R410.26)

**Identifying and Evaluating Threats**

- R410.4** Before a firm or network firm accepts an audit or any other engagement for an audit client, the firm shall determine whether the threats to independence created by the fees proposed to the client are at an acceptable level. The firm shall also re-evaluate such threats where appropriate during the engagement period for the audit if circumstances change.

410.4 A1 When fees are negotiated with and paid by the audit client, this creates a self-interest threat and might create an intimidation threat to independence.

410.4 A2 Factors that are relevant in evaluating the level of threats created when fees for an audit or any other engagement are paid by the audit client include:

- Whether there is external review of the quality of the firm's audit work.
- The level of the fees and the extent to which they have regard to the resources required, taking into account the firm's commercial and market priorities and position.
- The involvement of those charged with governance in appointing the auditor and agreeing fees, and the apparent emphasis they and client management place on the quality of the audit and the overall level of the fees.
- Any linkage between fees for the audit and those for services other than audit, and the relative size of both elements.
- The extent of any dependency between the level of the fee for, and the outcome of, the service.
- The significance of the client, for example to the firm, network, partner or office.
- The nature of the client, for example whether the client is a public interest entity.

410.4 A3 The conditions, policies and procedures described in paragraph 120.12 A3 (particularly the existence of a quality management system designed and implemented by the firm in accordance with [proposed] ISQM 1) might also impact the evaluation of whether the threats to independence are at an acceptable level.

410.4 A4 The requirements and application material that follow identify circumstances which might need to be further evaluated when determining whether the threats are at an acceptable level. For those circumstances, application material includes examples of additional factors that might be relevant in evaluating the threats.

### **Level of Audit Fees**

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

410.5 A2 In addition to the factors identified in paragraph 410.4 A2, factors that are relevant in evaluating self-interest and intimidation threats created by the level of the audit fee paid by the audit client include:

- The firm's commercial rationale for the audit fee.
- Whether pressure has been or is being applied by the client to reduce the audit fee.

410.5 A3 Examples of actions that might be safeguards to address such threats include:

- Having an appropriate reviewer who was not involved in the audit engagement assess the reasonableness of the fee proposed having regard to the scope and complexity of the engagement.
- Having an appropriate reviewer who was not involved in the audit engagement review the work undertaken.

Impact of Other Services Provided to an Audit Client

**R410.6** A firm shall not allow 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.

**410.6 A1** The audit fee ordinarily reflects a combination of matters, such as those identified in paragraph 410.22 A1. However, the provision of other services to the audit client is not an appropriate consideration in determining the audit fee.

**410.6 A2** Paragraph R410.6 is not intended to prohibit cost savings that can be achieved as a result of experience derived from the provision of services other than audit to the audit client.

**Contingent Fees**

**410.7 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 charged through an intermediary is an example of an indirect contingent fee. In this section, a fee is not regarded as being contingent if established by a court or other public authority.

**R410.8** A firm shall not charge directly or indirectly a contingent fee for an audit engagement.

**R410.9** A firm or network firm shall not charge directly or indirectly a contingent fee for a non-assurance service provided to an audit client, if:

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

**410.9 A1** Paragraphs R410.~~8~~ and R410.~~9~~ preclude a firm or a network firm from entering into certain contingent fee arrangements with an audit client. Even if a contingent fee arrangement is not precluded when providing a non-assurance service to an audit client, it might still impact the evaluation of the level of the self-interest threat~~a self-interest threat might still be created.~~

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

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

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

- Having an appropriate reviewer who was not involved in performing the non-assurance service review the work performed by the firm.

- Obtaining an advance written agreement with the client on the basis of remuneration.

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

410.10 A1 The evaluation of the level of the self-interest threat might be impacted when a large proportion of fees charged by the firm or network firms to an audit client is generated by providing services other than audit to the client, due to concerns about the potential loss of either the audit engagement or other services. Such circumstances might also create an intimidation threat. A further consideration is a perception that the firm or network firm focuses on the non-audit relationship, which might create a threat to the auditor's objectivity.

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

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

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

### **Total Fees – Overdue Fees**

410.11 A1 The evaluation of the level of the self-interest threat might be impacted if fees payable by the audit client for the audit or services other than audit are overdue during the period of the audit engagement. ~~A self-interest threat might be created if a significant part of fees is not paid before the audit report for the following year is issued.~~

410.11 A2 It is generally expected that the firm will ~~obtain~~ require payment of such fees before ~~the such~~ audit report is issued. ~~The requirements and application material set out in Section 511 with respect to loans and guarantees might also apply to situations where such unpaid fees exist.~~

410.11 A3 Factors that are relevant in evaluating the level of such a self-interest threat include:

- The significance of the overdue fees to the firm.
- The length of time the fees have been overdue.
- The firm's assessment of the ability and willingness of the client to pay the overdue fees.

410.11 A4 Examples of actions that might be safeguards to address such a self-interest threat include:

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

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

- (a) Whether the overdue fees might be equivalent to a loan to the client in which case the requirements and application material set out in section 511 are applicable; and
- (b) Whether it is appropriate for the firm to be re-appointed or continue the audit engagement.

**Total Fees – Fee Dependency**~~Relative Size~~

All Audit Clients ~~All Audit Clients~~

410.~~133~~ A1 When the total fees generated from an audit client by the firm expressing the audit opinion represent a large proportion of the total fees of that firm, the dependence on ~~that client~~ and concern about the potential loss of fees from audit and other services from that client~~losing the client~~ impact the evaluation of the level of the ~~create a~~ self-interest threat and create an ~~or~~ intimidation threat.

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

410.~~133~~ A~~32~~ Factors that are relevant in evaluating the level of such threats include:

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

410.~~133~~ A~~43~~ An ~~Ex~~amples of an ~~an~~ actions that might be a ~~a~~ safeguards to address such a ~~a~~ self-interest and/or ~~and/or~~ intimidation threats include ~~is~~

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

410.~~133~~ A~~54~~ 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.~~133~~ A~~65~~ Factors that are relevant in evaluating the level of such threats include:

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



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

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

#### Audit Clients that are Not Public Interest Entities

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

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

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

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

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

#### Audit Clients that are Public Interest Entities

**R410.174** When for each of two consecutive years the total fees from an audit client that is a public interest entity represent, or are likely to represent, more than 15% of the total fees received by the firm, the firm shall determine whether, prior to the audit opinion being issued on the second year's financial statements, an engagement quality review performed by a professional accountant who is not a member of the firm expressing the opinion on the financial statements ("pre-

~~issuance review”) might be a safeguard to reduce the threats to an acceptable level, and if so, apply it. Where an audit client is a public interest entity and, for two consecutive years, the total fees from the client and its related entities represent more than 15% of the total fees received by the firm expressing the opinion on the financial statements of the client, the firm shall:~~

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

~~**R410.5** When the total fees described in paragraph R410.4 significantly exceed 15%, the firm shall determine whether the level of the threat is such that a post-issuance review would not reduce the threat to an acceptable level. If so, the firm shall have a pre-issuance review performed.~~

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

- ~~(a) Disclose to and discuss with those charged with governance the matters set out in paragraph R410.; and~~
- ~~(b) Comply with paragraphs R410.4() and R410.5.~~

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

- ~~(a) The circumstances addressed by paragraph R410.17 apply to only one of the firms expressing the audit opinion; and~~
- ~~(b) Each firm performs sufficient work to take full individual responsibility for the audit opinion.~~

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

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

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

in the public interest; and

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

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

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

#### *Communication About Fee-related Information with Those Charged with Governance*

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

#### Audit Fees

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

- (a) The level of the fee for the audit of the financial statements on which the firm issued an opinion;
- (b) Any fees for the audit of special purpose financial statements and review engagements; and
- (c) Whether the threats created by the level of the audit fees are at an acceptable level and any actions the firm has taken or proposes to take to reduce such threats to an acceptable level.

410.22 A1 The objective of such communication is to provide the background and context to the audit fee to enable those charged with governance to consider the independence of the firm. The nature and extent of matters to be communicated will depend on the facts and circumstances and might include for example:

- Considerations affecting the level of the fee such as:
  - The scale, complexity and geographic spread of the audit client's operations.
  - The time spent or expected to be spent commensurate with the scope and complexity of the audit.
  - The cost of other resources utilized or expended in performing the audit.
  - The quality of record keeping and processes for financial statements preparation.
- Adjustments to the fee quoted or charged during the period of the audit, and the reasons for any such adjustments.
- Changes to laws and regulations and professional standards relevant to the audit that

impacted the fee.

410.22 A2 The firm is encouraged to provide such information as soon as practicable and communicate proposed adjustments as appropriate.

#### Fees for Services Other than Audit

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

**(a)** The fees charged during the period covered by the financial statements for the provision by the firm or a network firm of services other than audit to the client which for this purpose shall include only related entities over which the client has direct or indirect control; and

**(b)** Where the firm has identified that there is an impact on the evaluation of the level of the self-interest threat or that there is an intimidation threat to independence created by the proportion of such fees relative to the audit fee:

**(i)** Whether such threats are at an acceptable level; and

**(ii)** If not, any actions that the firm has taken or proposes to take to reduce such threats to an acceptable level.

410.23 A1 The objective of such communication is to provide the background and context to the fees for services other than audit to enable those charged with governance to consider the independence of the firm. The nature and extent of matters to be communicated will depend on the facts and circumstances and might include for example:

- The amount of fees from services other than audit that are required by laws and regulations.
- The nature of other services provided and their associated fees.
- Information on the nature of the services provided under a general policy approved by those charged with governance and associated fees.
- The proportion of fees referred to in paragraph R410.23(a) to the aggregate of the audit fees charged by the firm and network firms.

#### Fee Dependency

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

**(a)** That fact and whether this situation is likely to continue;

**(b)** The safeguards applied to address the threats created, including, where relevant, the use of a pre-issuance review (Ref: Para R410.17); and

**(c)** Any proposal to continue as the auditor under paragraph R410.20.

Public Disclosure of Fee-related Information

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

**(a)** Subject to paragraph R410.26, the fee for the audit of the financial statements on which the firm issued an opinion, comprising

(i) Fees paid or payable to the firm and network firms, and

(ii) Actual or estimated fees paid or payable to other firms that have performed audit procedures on the engagement;

**(b)** The total amount of fees charged during the period covered by the financial statements for the provision of services by the firm or a network firm to the audit client, which, for this purpose shall include only related entities over which the client has direct or indirect control, other than as disclosed under (a); and

**(c)** If applicable, the fact that the total fees received by the firm from the audit client represent, or are likely to represent, more than 15% of the total fees received by the firm for two consecutive years, and the year that this situation first arose.

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

**410.25 A1** The fees disclosed usually reflect the fees paid or estimated to be paid for the services based on the information available at the time of the disclosure. The fees paid or estimated to be paid for the audit engagement include all such fees paid or payable to firms in relation to the audit work performed on which the audit opinion is based.

**410.25 A2** An example of when compliance with laws and regulations would not substantively satisfy paragraph R410.25 is in the case of disclosure of fees for services other than audit, the exclusion of fees for services provided by network firms to the audit client and related entities over which the client has direct or indirect control.

**410.25 A3** Such information might be disclosed,

(a) By the audit client in its financial statements, annual report or proxy statement, or

(b) If not by the audit client, by the firm in a manner deemed appropriate for the circumstances.

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

**410.25 A5** The firm might also discuss with the client whether disclosure of other information relating to fees might enhance the users' understanding of the fees paid or payable and how they might influence the firm's independence. The nature and extent of matters to be considered will depend on the facts and circumstances and might include for example:

- Comparative information for the prior year's fees for audit and services other than audit.
- The nature of services and their associated fees as disclosed under paragraph R410.25(b).

- Safeguards applied when the total fees from the client represent or are likely to represent 15% of the total fees received by the firm.

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

**R410.26** As an exception to paragraph R410.25(a), where the audit client does not make the disclosure specified in R410.25(a) and the firm is not able to obtain or provide an estimate of the fees referred to in paragraph R410.25(a)(ii), the firm shall be satisfied that the fee information that is available is publicly disclosed together with an explanation, to the extent possible, of the qualitative significance of the fee information which is not available.

Considerations for Review Clients

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

## PART 4B – INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

### SECTION 905

#### FEES

##### Introduction

- 905.1 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.
- 905.2 ~~The nature and level of Fees or other types of remuneration might create a self-interest or intimidation threat. This section sets out specific requirements and application material relevant to applying the conceptual framework to identify, evaluate and address threats to independence arising from fees charged to assurance clients in such circumstances.~~

##### Requirements and Application Material

###### Identifying and Evaluating Threats

- R905.3** ~~Before a firm accepts an assurance engagement, the firm shall determine whether the threats to independence created by the fees proposed to the assurance client are at an acceptable level. The firm shall also re-evaluate such threats where appropriate during the engagement period if circumstances change.~~
- 905.3 A1 ~~When fees are negotiated with and paid by the assurance client, this creates a self-interest threat and might create an intimidation threat to independence.~~
- 905.3 A2 ~~Factors that are relevant in evaluating the level of threats created when fees are paid by the assurance client include:~~
- ~~• The nature of the assurance engagement.~~
  - ~~• Whether there is external review of the firm's system of quality management.~~
  - ~~• The level of the fees for the assurance engagement and the extent to which they have regard to the resources required, taking into account the firm's commercial and market priorities and position.~~
  - ~~• The extent of any dependency between the level of the fee for, and the outcome of, the service.~~
  - ~~• The significance of the client for example to the firm or partner.~~
  - ~~• The nature of the client.~~
- 905.3 A3 ~~The conditions, policies and procedures described in paragraphs 120.12 A3 (particularly the existence of a quality management system designed and implemented by a firm in accordance with [proposed] ISQM 1) might also impact the evaluation of whether the threats to independence are at an acceptable level.~~
- 905.3 A4 ~~The requirements and application material that follow identify circumstances which might need to be further evaluated when determining whether the threats are at an acceptable level. For~~

those circumstances, application material includes examples of additional factors that might be relevant in evaluating the threats.

### **Level of Fees for Assurance Engagements**

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

905.4 A2 In addition to factors identified in paragraph 905.3 A2, factors that are relevant in evaluating self-interest and intimidation threats created by the level of the fee for an assurance engagement when paid by the assurance client include:

- The firm's commercial rationale for the fee for the assurance engagement.
- Whether pressure has been or is being applied by the client to reduce the fee for the assurance engagement.

905.4 A3 Examples of actions that might be safeguards to address such threats include:

- Having an appropriate reviewer who was not involved in the assurance engagement assess the reasonableness of the fee proposed having regard to the scope and complexity of the engagement.
- Having an appropriate reviewer who was not involved in the assurance engagement review the work.

### **Contingent Fees**

905.5 A1 Contingent fees are fees calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed. A contingent fee charged through an intermediary is an example of an indirect contingent fee. In this section, a fee is not regarded as being contingent if established by a court or other public authority.

**R905.6** A firm shall not charge directly or indirectly a contingent fee for an assurance engagement.

**R905.7** A firm shall not charge directly or indirectly a contingent fee for a non-assurance service provided to an assurance client if the outcome of the non-assurance service, and therefore, the amount of the fee, is dependent on a future or contemporary judgment related to a matter that is material to the subject matter information of the assurance engagement.

905.7 A1 Paragraphs R905.~~67~~ and R905.~~78~~ preclude a firm from entering into certain contingent fee arrangements with an assurance client. Even if a contingent fee arrangement is not precluded when providing a non-assurance service to an assurance client, it might still impact the evaluation of the level of the self-interest threat~~a self-interest threat might still be created.~~

905.7 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 subject matter information.

905.7 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 relevant assurance work.
- Obtaining an advance written agreement with the client on the basis of remuneration.

**Total Fees—Overdue Fees**

905.8 A1 ~~The evaluation of the level of the self-interest threat might be impacted if fees payable by the assurance client for the assurance engagement or other services are overdue during the period of the assurance engagement. A self-interest threat might be created if a significant part of fees is not paid before the assurance report, if any, for the following period is issued. It is generally expected that the firm will require payment of such fees before any such report is issued. The requirements and application material set out in Section 911 with respect to loans and guarantees might also apply to situations where such unpaid fees exist.~~

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

- The significance of the overdue fees to the firm.
- The length of time the fees have been overdue.
- The firm's assessment of the ability and willingness of the client or other relevant party to pay the overdue fee.

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

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

**R905.9** When a significant part of fees due from an assurance client remains unpaid for a long time, the firm shall determine:

- Whether the overdue fees might be equivalent to a loan to the client in which case the requirements and application material set out in Section 911 are applicable; and
- Whether it is appropriate for the firm to be re-appointed or continue the assurance engagement.

**Total Fees—~~Fee Dependency~~Relative Size**

905.~~103~~ A1 When the total fees generated from an assurance client by the firm expressing the conclusion in an assurance engagement represent a large proportion of the total fees of that firm, the dependence on ~~that client~~ and concern about the potential loss of fees from that client impact the evaluation of the level of the losing the client create a self-interest threat and create an or intimidation threat.

905.10 A2 ~~A self-interest and intimidation threat is created in the circumstances described in paragraph 905.10 A1 even if the assurance client is not responsible for negotiating or paying the fees for the assurance engagement.~~

905.10 A3 In calculating the total fees of the firm, the firm might use financial information available from the previous financial year and estimate the proportion based on that information if appropriate.

905.~~103~~ A~~42~~ Factors that are relevant in evaluating the level of such threats include:

- The operating structure of the firm.
- The qualitative and quantitative significance of the assurance client to the firm.
- Where the firm is expected to expand such that the significance of the client is likely to reduce.
- ~~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.~~

905.~~103~~ A~~53~~ ~~An~~ Examples of ~~an~~ actions that might be ~~a~~ safeguards to address such a self-interest ~~and or~~ intimidation threats ~~is~~ include:

- Reducing the extent of services other than assurance engagements provided to the client.
- Increasing the client base in the firm to reduce dependence on the assurance client.

905.~~103~~ A~~64~~ A self-interest or intimidation threat is also created when the fees generated by the firm from an assurance client represent a large proportion of the revenue from an individual partner's clients.

905.10 A7 Factors that are relevant in evaluating the level of such threats include:

- The qualitative and quantitative significance of the assurance client to the partner.
- The extent to which the compensation of the partner is dependent upon the fees generated from the client.

905.~~103~~ A~~85~~ Examples of actions that might be safeguards to address such a self-interest or intimidation threat include:

- Having an appropriate reviewer who was not an assurance team member review the work.
- Ensuring that the compensation of the partner is not significantly influenced by the fees generated from the assurance client.
- Increasing the client base of the partner to reduce dependence on the ~~assurance~~-client.

**PROPOSED CONSEQUENTIAL AND CONFORMING AMENDMENTS**  
**(MARK-UP FROM EXTANT CODE)**

**SECTION 120**

**THE CONCEPTUAL FRAMEWORK**

....

**Considerations for Audits, Reviews and Other Assurance Engagements**

*Independence*

120.12 A1 Professional accountants in public practice are required by International Independence Standards to be independent when performing audits, reviews, or other assurance engagements. Independence is linked to the fundamental principles of objectivity and integrity. It comprises:

- (a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.
- (b) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude that a firm’s or an audit or assurance team member’s integrity, objectivity or professional skepticism has been compromised.

120.12 A2 International Independence Standards set out requirements and application material on how to apply the conceptual framework to maintain independence when performing audits, reviews or other assurance engagements. Professional accountants and firms are required to comply with these standards in order to be independent when conducting such engagements. The conceptual framework to identify, evaluate and address threats to compliance with the fundamental principles applies in the same way to compliance with independence requirements. The categories of threats to compliance with the fundamental principles described in paragraph 120.6 A3 are also the categories of threats to compliance with independence requirements.

120.12 A3 Conditions, policies and procedures described in paragraphs 120.6 A1 and 120.8 A2 that might assist in identifying and evaluating threats to compliance with the fundamental principles might also be factors relevant to identifying and evaluating threats to independence. In the context of audits, reviews and other assurance engagements the existence of a quality management system designed and implemented by a firm in accordance with [proposed] ISQM 1 is an example of such conditions, policies and procedures.

## 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 does not allow for sufficient and appropriate resources (including human, technological and intellectual property resources) to perform the services in accordance with technical and 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 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 technical and 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:
- (c) Whether the client is aware of the terms of the engagement and, in particular, the basis on which fees are determined ~~charged~~ and which professional services are the quoted fee covered ~~eds~~.
  - (d) 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.

## 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.
- The level of fees and the extent to which they have regard to the resources required, taking into account the professional accountant's commercial and market priorities and position.

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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