

PROJECT PROPOSAL — FEES

I. Subject

1. The fee-related provisions in the IESBA's *International Code of Ethics for Professional Accountants (including International Independence Standards)* (the Code).

II. Background and Relevant Developments

2. In its [Strategy and Work Plan 2014-2018](#), the IESBA committed to undertaking work to further understand a number of fee-related matters in response to feedback from the regulatory community, and in particular, the International Organization of Securities Commissions (IOSCO), and the changing global environment. In approving the IESBA's April 2015 pronouncement, [Changes to the Code Addressing Certain Non-Assurance Services Provisions for Audit and Assurance Clients](#), the Public Interest Oversight Board (PIOB) asked the IESBA to revisit issues on auditor independence and "non-audit services" more broadly, including fee-related matters. In response, the IESBA resolved to bring forward its fee-related initiative, which was initially planned to commence in 2017, and established the Fees Working Group (WG) in July 2015.
3. The WG's objective, under its [Terms of Reference](#), was to undertake fact finding in the following areas with a view to identifying whether there is a relationship between fees and threats to compliance with the fundamental principles or to independence, or whether there are reasonable perceptions that such threats exist, as well as how such threats might be addressed:
 - (a) Level of audit fees for individual audit engagements (level of fees).
 - (b) Relative size of fees¹ to the partner, office or the firm, and the extent to which partners' remuneration is dependent upon fees from a particular client (fee dependency).
 - (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).
4. The WG's fact finding activities included:
 - (a) A high level review of the relevant fee provisions in a number of G-20 jurisdictions (G-20 benchmarking);
 - (b) A review of relevant academic research and other literature; and
 - (c) Outreach to stakeholders to obtain their perspectives about the fee-related matters (stakeholder outreach).
5. The [G-20 benchmarking](#), presented to the IESBA in December 2016, highlighted that some jurisdictions have more specific provisions in relation to the level of fees, fee dependency and the ratio of non-audit services fees to audit fees.
6. To review relevant academic research and other literature, the IESBA commissioned Prof. David Hay, Professor of Auditing, University of Auckland, New Zealand. The scope of Prof. Hay's work was

¹ This will consider total fees.

limited to a review of existing studies on audit fees between 2006 and 2016 and did not include any quantitative meta-analysis of those studies or examination of primary data. With regard to each of the four areas of focus, in December 2016 Prof. Hay's presented the IESBA his observations in his [final report](#).

7. As the third key fact finding element of this initiative, the IESBA agreed to the use of a questionnaire to gather further views from stakeholders with respect to the fee-related matters being explored by the WG. In November 2017, the questionnaire was published and 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.
8. At the June 2018 IESBA meeting, the WG presented its [final report](#) (final report) on the outcome of the fact finding activities. The report included the WG's recommended way forward with respect to the above four focus areas, with a fifth focus area identified from comments from IOSCO, i.e., fee-related safeguards in the Code.
9. On the basis of the final report, the IESBA asked the WG to develop a project proposal for potential enhancements to the Code in relation to the topic of fees, and as part of this project, update the staff publication on [Ethical Considerations Relating to Audit Fee Setting in the Context of Downward Fee Pressure](#) to align it with the Code. The IESBA also asked the WG to coordinate its work related to overlapping issues with other IESBA Working Groups and Task Forces and with the International Auditing and Assurance Standards Board (IAASB).

III. Project Objective and Scope, and How the Project Serves the Public Interest

Project Objective

10. To review the provisions in the Code as these pertain to fee-related matters within the project scope, and recommend any changes considered necessary for the Code to remain robust and appropriate in enabling professional accountants to meet their responsibility to comply with the fundamental principles and, where applicable, be independent.

Project Scope

11. The scope of the project encompasses the following specific areas:
 - (a) A review of the provisions in Part 3 of the Code with respect to the level of audit fees for individual audit engagements, and in Part 2 in considering the role of professional accountants in business (PAIB) in approving the level of audit fees;
 - (b) A review of the provisions in Part 4A of the Code with respect to (total) fee dependency at a firm, office and partner level for all audit clients, including considering the introduction of a specific threshold for audit clients which are not public interest entities (PIE) ; and
 - (c) A review of the safeguards in the Code pertaining to the scope of this project.
12. Although the final report discussed the level of fees without being explicit as to the type of work being considered, the WG notes that its objectives and the scope of its fact finding activities were focused on the level of audit fees as a matter of public interest. In addition, no concerns were raised by stakeholders regarding the level of fees for other types of engagement. It is therefore proposed that the project will only examine the issue of the level of fees for individual audit engagements, as set out in para 11(a) above.

13. For reasons mentioned above, the project will focus on fee dependency in relation to audit clients. For the purpose of maintaining consistency between fee-related provisions of Part 4A and Part 4B of the Code, the Task Force will consider any consequential changes that may be required to Part 4B.
14. The Appendix includes additional information on two further issues, from the final report presented by the WG in June 2018, that are outside the scope of this project but the Board has decided these might be addressed by other IESBA Working Groups or by the IESBA Planning Committee:
 - (a) Ethical and independence considerations relating to the ratio of non-audit services fees to audit fees paid by an audit client; and
 - (b) Ethical and independence implications of the business model of firms.
15. The project will involve a consideration of any other matters that are deemed relevant to achieve the objective of the project.

How the Project Serves the Public Interest

16. Fees are a significant factor that influence the behavior of professional accountants. The project will serve the public interest through ensuring that:
 - (a) The provisions in the Code continue to be robust and appropriate in enabling professional accountants to address threats to compliance with the fundamental principles and to independence created by
 - The level of audit fees charged to audit clients; and
 - The undue fee dependency at the firm, office and partner levels from one audit client; and
 - (b) The safeguards in the Code are clear, appropriate and effective in addressing fee-related issues.
17. Professional accountants' independence and compliance with the fundamental principles contribute to audit quality, thereby increasing the credibility of financial information in respect of which they are engaged to express audit opinions.

IV. Matters of Coordination

Coordination with IAASB

18. A specific plan for coordination with the IAASB will be developed as this project gets under way, pursuant to the IESBA's strategic commitment to engage in close coordination with the IAASB on matters of mutual interest. In particular, consideration will be given to how best to address coordination on issues that might overlap with topics addressed under ISQC 1², ISA 220³ and ISA 600⁴.

² International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*

³ International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

⁴ ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

Coordination with Other IESBA Working Groups or Task Forces

19. The Task Force will coordinate its work with the work of the NAS Working Group (or any Task Force subsequently established) to the extent that there is a need to coordinate potential amendments to the Code or exchange information or perspectives on issues being addressed by the other Working Group or Task Force. Should the IESBA decide to initiate a work stream on the topic of firms' business model, the Task Force will also consider the need for coordination with any working group responsible for that work stream.

V. Outline of the Project

Issues that Will Be Addressed

Level of Audit Fees

20. In the period since the Fees Initiative was approved by the IESBA, the extant Code has been revised to include an enhanced conceptual framework to identify, evaluate and address threats to compliance with the fundamental principles⁵. In addition revised examples of actions that might be safeguards to threats to compliance with the fundamental principles and to independence have been included in the Code. These revisions, which also include updated safeguards, also affect the fee-related provisions of the extant Code.
21. Part 3 of the Code currently acknowledges that a professional accountant might quote whatever fee is considered appropriate. It states that quoting a fee lower than another accountant is not in itself unethical. 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.⁶ 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.⁷
22. In January 2016, the IESBA staff released the publication *Ethical Considerations Relating to Audit Fee Setting in the Context of Downward Fee Pressure*, which aims to highlight the auditor's ethical responsibilities under the extant Code when setting audit fees, especially in the circumstances of downward pressure on fees.
23. From its fact finding, the WG reported that there are reasonable perceptions that an unduly low level of audit fees could create threats to compliance with the fundamental principles and adversely impact audit quality. The WG further found that some jurisdictions have established rules or standards to emphasize clearly that fees charged must not be allowed to impair the auditor's ability to perform the audit engagement according to standards and regulations. The WG also noted suggestions from some stakeholders to consider the role of PAIBs⁸ who are involved in an entity's governance, as well as others who take part in decisions concerning the appointment and reappointment of auditors, particularly with respect to raising their awareness of the risks relating to fee pressure.

⁵ Integrity, Objectivity, Professional Competence and Due Care, Confidentiality, and Professional Behavior.

⁶ Part 3 – Professional Accountants in Public Practice, Section 330 *Fees and Other Types of Remunerations*, paragraph 330.3 A2

⁷ Paragraphs 330.3 A3-A4

⁸ The Code currently sets out requirements and application materials for PAIBs in Part 2, Section 270 related to pressure exerted on, or by, a professional accountant.

24. This project will therefore:
- (a) Review the responsibilities of the engagement partner and the firm for fees quoted to audit clients under the Code and determine whether there is a need for further enhancement to the Code;
 - (b) Review the responsibilities of PAIBs, whether in a governance role or otherwise, with respect to the level of audit fees when taking part in appointing or reappointing auditors, and determine whether there is a need to establish specific expectations of them in the Code in this regard;
 - (c) Consider whether the provisions in Part 3 of the Code⁹ related to level of fees quoted continue to be robust and appropriate, or whether they should be further strengthened; and
 - (d) Review the role of communication with TCWG, and the role of public disclosure in relation to audit fees, and determine whether there is a need to include provisions to the Code in this regard.
25. As part of this project, the IESBA has also commissioned IESBA Staff to update the staff publication, referred to in paragraph 9 above, to align it with the Code at the earliest opportunity.

Fee Dependency

26. In Part 4A, the Code states that when the total fees generated from an audit client by the firm expressing the audit opinion represent a large proportion of the total fees of that firm, the dependence on that client and concern about losing the client create a self-interest or intimidation threat (a similar provision is in Part 4B with respect to an assurance client).¹⁰ The WG will consider the need for consequential amendments to Part 4B should amendments be proposed to similar provisions in Part 4A.
27. 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).¹¹
28. In addition, for audit engagements, the Code includes disclosure requirements for firms and specific actions 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% of the firm's total fees for two consecutive years.¹²
29. On the topic of fee dependency, the WG found that there was no hard evidence to suggest that changing the threshold for the percentage of revenue generated from PIE clients in the Code will reduce threats to independence.
30. In most of the observed jurisdictions covered under the G-20 benchmarking, standards or regulation dealing with fee dependency at office and partner levels and the percentage of total revenue from PIE audit client align with the Code. However, a few IFAC member bodies and a regulator¹³ have

⁹ Part 3 – Professional Accountants in Public Practice

¹⁰ Paragraphs 410.3 A1 and 905.3 A1

¹¹ Paragraphs 410.3 A4 and 905.3 A4

¹² Paragraphs R410.4 – R410.6

¹³ Royal Netherlands Institute of Chartered Accountants, Wirtschaftsprüferkammer, UK Financial Reporting Council

indicated that in their jurisdictions, rules to address the fee dependency issue are more stringent than those in the Code.

31. In light of the approaches taken by some jurisdictions to addressing the fee dependency issue, the project will:
 - (a) Review the requirements and application material in the Code pertaining to fee dependency in relation to PIE and non-PIE audit clients;
 - (b) Review how threats relating to fee dependency for non-PIEs might be addressed, including for example through the use of thresholds.

Fee-related Safeguards

32. Taking into account the input from IOSCO¹⁴ during the stakeholder outreach, the project will review the fee-related safeguards in the Code to determine whether they are clear, appropriate and effective in addressing threats to compliance with the fundamental principles and to independence.

Impact Analysis Considerations

33. Should the fee-related provisions in the Code be further enhanced, the primary benefit would be to increase public trust in professional accountants who undertake audit engagements through strengthening their responses to threats to compliance with the fundamental principles, and to independence.
34. Depending on the nature and extent of any revisions to the Code as a result of this project, there may be implications with respect to implementation costs at the engagement or firm levels. Furthermore, those implications may vary depending on the size of the firms and the nature of the audits they perform. Appropriate consideration will be given to the likely costs and benefits of proposals developed.
35. Specific regard will be given to ensuring that proposals developed under this project do not give rise to conflicts with anti-competition laws around the world. Stakeholders will be specifically invited to share any concerns they might have in this regard as part of any formal consultation on proposals developed under this project.

VI. Implications for any Specific Persons or Groups

36. The project has 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.
37. The project is relevant to firms that provide audit and other assurance services, irrespective of their size. In particular, there will be a need for outreach to the Forum of Firms and the IFAC Small and Medium Practices (SMP) Committee to keep them informed on the developments and to ensure that appropriate input is received from them at all key stages of the project.
38. The project may also have implications for those charged with governance (TCWG), particularly PAIBs who take part in decisions regarding appointing and reappointing auditors, and for other PAIBs who have a role in negotiating or agreeing fees for audit engagements.

¹⁴ [Letter from IOSCO's Committee on Issuer Accounting, Audit and Disclosure dated March 20, 2018](#)

39. The project may also be relevant to other stakeholders in the financial reporting supply chain, in particular preparers as well as regulators in relation to the enforcement of independence requirements.

VII. Development Process, Project Timetable and Project Output

Development Process

40. The project will follow the normal due process of the IESBA for changes to the Code.

Project Timetable

41. Subject to the IESBA's approval of the project proposal, this project will commence immediately. The specific project milestones and outputs will depend on the matters that the Task Force determines are appropriate to proceed with for the purposes of the project, and the priorities assigned to those matters.
42. The Task Force will coordinate the timing of the project with the Non-Assurance Services project, once approved, as necessary, recognizing that certain areas of the projects are related.
43. The indicative timing for the project up until the issuance of an Exposure Draft is as follows:

Indicative Timing	Milestone
September 2018	<ul style="list-style-type: none">• Discussion of project proposal with IESBA CAG• IESBA approval of project proposal
March 2019	<ul style="list-style-type: none">• IESBA CAG and IESBA: Discussion of issues
June 2019	<ul style="list-style-type: none">• Discussion with national standard setters• First-read proposed changes to the Code
September 2019	<ul style="list-style-type: none">• Discussion with IESBA CAG• IESBA approval of Exposure Draft

Project Outputs

44. It is anticipated that the output of the project will include:
- New or revised requirements and application material in the Code relating to the matters identified within the scope of the project; and
 - An updated version of the January 2016 IESBA Staff publication on fees aligned to the Code.
45. Depending on the issues identified, the Task Force may also provide recommendations to the IESBA regarding:
- Commissioning of off-Code guidance (such as IESBA Staff publications) on relevant topics;
 - Issuing communications to convey key messages to stakeholders on fee-related issues.

VIII. Resources Required

46. A project Task Force will be established, consisting of four individuals, including an IESBA member as Chair.
47. IESBA Staff will provide support to the project Task Force.

IX. Relevant Sources of Information that Address the Matter Being Proposed

48. Relevant sources of information include:
 - Final Report of the Fees Working Group presented in June 2018 to the IESBA.
 - Relevant national ethics or independence standards pertaining to fees.
 - IAASB standards, and in particular ISQC 1.

Fee-related Matters to be Addressed by Other IESBA Working Groups or the Planning Committee

Ratio of Non-audit Services

1. Regarding the topic of ratio of non-audit services fees to audit fees, the WG's report noted that there is a reasonable perception that a high ratio of non-audit services fees to audit fees creates threats to independence, particularly threats to independence in appearance. Many jurisdictions have specific rules, mainly addressing 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 to address threats to independence in appearance.
2. While formulating its recommended way forward regarding how best to address threats related to the ratio of non-audit services fees to audit fees, the WG took into consideration that this topic is directly related to the scope of work of the IESBA's NAS Working Group. Accordingly, in the final report, it was proposed that this topic be addressed as part of the NAS work stream.
3. Based on the WG's report, options for the way forward that the NAS Working Group might consider include:
 - Requiring an assessment of the nature, frequency, value and cumulative effect of non-audit services on independence when providing multiple non-audit services to audit clients.
 - Considering the role of disclosure of fee-related information to stakeholders, including public disclosure.
 - Considering enhanced provisions relating to communication with TCWG, including seeking pre-approval of non-audit services, as was also suggested by the PIOB.
 - Considering provisions that would require firms to re-evaluate threats to independence when the ratio of NAS fees to audit fees reach a particular threshold.
 - Hard-wiring in the Code a cap on the level of fees for non-audit services in relation to audit fees, and whether caps should be set in relation to both PIEs and non-PIEs.

Business Model

4. From the academic research, there was no firm evidence that the provision of audit services by a firm that also has a significant non-audit services business creates threats to compliance with the fundamental principles and to independence. Further, at this time, there is no indication that jurisdictions have developed standards or regulation to address this issue.
5. The IESBA considers the issue of the business model is a complex, multi-faceted topic in respect of which there is a need for robust engagement among all key players, including standard-setting boards, regulators, investors, the corporate governance community, preparers, national standard setters, firms, the academic community and IFAC member bodies. As part of this multi-stakeholder engagement, the WG proposes that the Planning Committee give consideration to the IESBA initiating a dialogue with the IAASB on how best to develop a way forward on this topic.