

## AGENDA PAPER

**Item Number:** 11

**Date of Meeting:** 3 June 2022

**Subject:** Proposed revisions to APES 110 for Fee-related provisions of the Code.

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**Action required**     **For discussion**     **For noting**     **For information**

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### Purpose

To obtain the Board's:

- (a) views on the suggested revisions to the proposed amendments in ED 01/22 *Proposed amendments to Fee-related provisions of APES 110 Code of Ethics for Professional Accountants (including Independence Standards)* (ED 01/22); and
- (b) approval to issue an amending standard containing revisions to the fee-related provisions of APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code).

### Background

On 28 April 2021, the IESBA issued the final pronouncement *Revisions to the Fee-related Provisions of the Code*. The changes, which are effective from 15 December 2022, are to the provisions of the *International Code of Ethics for Professional Accountants (including International Independence Standards)* (the IESBA Code).

Locally, in 2019, a Parliamentary Joint Committee (PJC) Inquiry commenced considering audit regulation in Australia. The PJC held public hearings in 2019 and 2020 and issued an interim report in February 2020 and a final report in November 2020. At the date of writing this report, the Federal Government is yet to release a response to the PJC's recommendations.

In May 2021, APESB issued Exposure Draft (ED) 03/21 *Proposed Amendments to Fee-related provisions of APES 110 Code of Ethics for Professional Accountants (including Independence Standards)* (ED 03/21) with a comment period that closed on 31 August 2021.

APESB received 19 submissions from a broad range of respondents, including small-to-medium-practices (SMPs), mid-to-large accounting firms, professional organisations and regulators. The submissions generally supported the proposals in the exposure draft, apart from concerns with the proposed revisions relating to fee dependency on a referral source.

At the March 2022 Board meeting, the Board considered the outcomes from the exposure draft due process. The Board:

- discussed the proposed amendments based on revisions to the IESBA Code and considered the implementation of these provisions when the language used is different from the *Corporations Act 2001* and Australian Accounting Standards.
- approved the amendments to revise the audit partner incentivisation provisions and update references to the reissued APES 320 *Quality Management for Firms that Provide Non-Assurance Services* (APES 320).
- agreed to defer the inclusion of audit fee categories in the Code to ensure consistency with the outcomes of the AASB project on audit fee disclosures; and
- agreed to re-expose the proposed amended provisions relating to fee dependency on a referral source, including potential options for the actions that a member in public practice should take if the fee dependency threshold of 30% continues for five consecutive years.

## Key Considerations

To facilitate the consideration of the proposed amendments to the fee-related provisions of the Code, the discussion below is structured based on the driver for change of the proposed amendments (i.e., IESBA Code or regulators' requests). The paper will not reconsider the matters (e.g., audit partner incentivisation provisions and APES 320 reference updates) that the Board approved at the March 2022 Board Meeting.

The proposed Amending Standard on Fees is set out at agenda Item 11 (a) and contains mark-ups of amendments to the provisions from the proposals set out in the exposure drafts ED 03/21 and ED 01/22.

### a) **The IESBA Final Pronouncement: Revisions to the Fee-related provisions of the Code**

The majority of the proposed revisions to the Code are based on the IESBA's final pronouncement on fees, with minor editorial amendments (which were approved by the Board at the May 2021 Board Meeting for inclusion in the exposure draft).

The Board considered the results of the due process on ED 03/21 at the March 2022 Board Meeting. At that meeting, it was noted that respondents were generally supportive of the proposed revisions based on the IESBA pronouncements, and the provisions were considered for adoption without further amendment. However, the Board discussed the implementation of the new IESBA provisions when the language used is not consistent with the requirements to disclose audit fees under the *Corporations Act 2001* and the Australian Accounting Standards, and requested that further consideration occur on this matter.

Technical Staff have reviewed the information provided by a stakeholder on the potential issues surrounding the different language used in Australian regulations compared to the IESBA provisions on disclosure of audit fees. As part of the information provided by the stakeholder, APESB was requested to consider whether the fee disclosure requirements in the Australian laws and regulations substantively satisfy the requirements and achieve the objectives of the provisions to achieve transparency of fee-related information in R410.23(a), R410.25(a) and R410.31(a) and (b). The stakeholder then requested that if APESB believed that was the case, would it consider the addition of an Australian provision or a footnote that provides that:

- the laws and regulations that apply to the disclosure of fee-related information contained in the Australian Accounting Standards and the Corporations Act

substantively satisfy the requirements for audit client disclosure contained in R410.31(a) and (b); and

- in respect of companies required to comply with these laws and regulations, firms in Australia meet the requirements of R410.23(a) and R410.25(a) by communicating information to the audit client consistent with the corresponding client disclosure laws and regulations in Australia.

Technical Staff have researched this matter and noted that the issues of different terms being used between professional standards and the regulations, and what 'substantially the same' means was raised in a [submission made by Deloitte](#) in June 2020 on the relevant IESBA exposure draft on fee-related provisions in the Code.

The IESBA, in paragraphs 108 and 121 of the [Basis for Conclusions](#) for their final Fees pronouncement, note the consideration of these issues raised by stakeholders. The IESBA determined that a principles-based approach to public disclosure would be better than a prescriptive approach. It allows the firms more flexibility to meet the necessary transparency disclosures by using their professional judgment. The IESBA also reiterated that the disclosures are not so much about the comparability of audit fees across different entities and groups as they are about transparency and an auditor's independence. APESB Technical Staff agree with the comments made by the IESBA about these issues.

In relation to the disclosures being made by the auditor, APESB Technical Staff note that the communication with Those Charged with Governance on audit fees for the financial statements (proposed paragraph R410.23) and other fees received by the auditor for the audit period (proposed paragraph R410.25) for audit clients that are public interest entities (PIEs) is about whether the level of the fees has created a threat to their independence.

This is very similar to the requirement in paragraph 17 of the [Auditing Standard ASA 260 Communication With Those Charged With Governance](#), whereby auditors of listed entities should communicate with Those Charged with Governance about relevant ethical requirements regarding independence, including the level of fees charged during the period so that those charged with governance can assess the effect of the fees and services on the independence of the auditor. As there is existing guidance on this required communication, APESB Technical Staff do not believe additional provisions or a footnote are required in relation to proposed paragraphs R410.23 and R410.25 to assist auditors in using their professional judgement to determine if the communication requirements have been met.

The disclosures required under proposed paragraph R410.31 require a Firm to publicly disclose information on audit fees, fees for other services, or fee dependency information for their PIE audit clients if the Audit Client does not make those disclosures. Proposed paragraph R410.30 notes that if the disclosures are not required by law and regulations, the auditor should first discuss this with Those Charged with Governance.

In ED 03/21. APESB Technical Staff proposed the inclusion of a footnote to this paragraph which refers to the disclosures required to be made by Those Charged with Governance information concerning fees paid to the external auditor and auditor independence under local laws and regulations.

APESB Technical Staff does not support the inclusion of a further additional Australian provision or footnote which confirms that the disclosure requirements of the audit client under local laws and regulations concerning fees paid to the auditor would meet the disclosure requirements of the auditor in relation to the transparency of any threats to independence caused by the level of fees charged to the client.

The reasons for this view are:

- APESB does not provide advice on how its pronouncement should be interpreted in practice (as per paragraph 7.2 of APESB's *Due process and working procedures for the development and review of APESB pronouncements*).
- It may be perceived that APESB is interpreting another Standards Setter's documents or legislation and commenting on the intent of the relevant provisions;
- APESB's standard drafting practice in the Code is to provide a cross-reference to applicable standards and legislation and leave it to the professional judgement of the Firm or Member to apply it to their circumstances; and
- There would be a risk of unintended consequences if APESB expressed a definitive view on the parity of Accounting and Auditing Standards, laws and regulations to the Code.

Technical Staff seek the Board's approval of the revisions to the Code based on the IESBA pronouncement on fees without any further amendments.

**b) Inclusion of a threshold in relation to fee dependency on a referral source of multiple audit clients (SMSF issues)**

After receiving a request from regulators, the Board agreed to include in ED 03/21 a proposal to introduce a 20% threshold (rather than using the term 'a large proportion') to assess fee dependency from a referral source at a firm, an office or a partner level.

The respondents' views on the initial proposals were mixed, with respondents generally supportive of the provision of guidance, but there were concerns about how the requirements would be implemented and enforced in practice. Further engagement with stakeholders helped APESB Technical Staff develop revised provisions on fee dependency on a referral source which included:

- An increase of the proposed threshold to 30% (up from 20%);
- The factor of a five-year cumulative time period to be met before the requirement is to be applied;
- The firm must take a definitive action (such as a review or a compliance engagement) at the five-year mark; and
- An additional requirement to clarify the position of fee dependency past the initial five-year cumulative period.

The drafting of the revised revisions was based on the IESBA provisions for fee dependency concerns for a single non-PIE audit client (proposed paragraphs R410.15 and R410.16) to ensure that the threats associated with fee dependency are treated consistently, whether the dependency is from one referral source or one audit client.

Technical Staff believed further consideration was needed as to what specified action should be undertaken if fee dependency is in place for five consecutive years.

Technical Staff identified three potential options for actions that could be undertaken, as follows:

1. have an appropriate reviewer who was not involved in the audit engagement review the audit work (which is a suggested safeguard in proposed paragraph 410.14 A7);
2. require a review to be completed in line with the guidance in *ASQM 2 Engagement Quality Reviews*; or
3. perform a compliance engagement to provide assurance that the fee dependency does not impact the audit's performance.

The revised provision and the proposed options for the action to be undertaken were re-exposed for stakeholder feedback in ED 01/22.

APESB received seven submissions from stakeholders concerning the proposals in ED 01/22. The submissions from six stakeholders are tabulated in a General Comments Table and Specific Comments Table at Agenda Items 11 (c) and 11 (d), respectively. In addition, the confidential submission from the Australian Taxation Office (ATO) is included at Agenda Item 11 (f) for the Board's consideration only.

Stakeholders were generally supportive of the proposed changes to the re-exposed provisions addressing fee dependency on a referral source. In particular, most stakeholders supported the proposed 30% threshold and the requirement that addresses the situation where fee dependency extends for greater than five years.

There were mixed views from stakeholders about the proposed five-year time period and whether this provides too much time before SMSF Auditors need to address fee dependency. Technical Staff acknowledge that five years is a long time before the provision comes into effect. However, no stakeholder provided compelling evidence as to why the time period should be shorter than the time period used in assessing fee dependency for a single non-PIE audit client (proposed paragraph R410.15). It is also important to note that the conceptual framework requires Members to identify, evaluate and address threats to independence when it is necessary. Members who have identified that they are dependent on fees from a referral source over a couple of years, should be alert to the need to consider how this impacts their independence using the overarching requirement to apply the conceptual framework to address threats to the fundamental principles and independence.

Stakeholders also provided mixed views in relation to the proposed options for actions to be taken after five years of fee dependency. Most stakeholders supported option 1, which would be to have an appropriate reviewer who was not involved in the audit engagement review the audit work. However, a couple of stakeholders suggested that all options could be included to provide flexibility to the reviewer to determine what engagement should be performed.

In considering which option to implement, Technical Staff have considered the need to clarify what a review entails (which was raised by SMP practitioners in their submissions) without imposing a significant compliance burden. Technical Staff are of the view that Option 1 should be adopted in the Code. This option allows the practitioner to determine the work that needs to be performed without the need for the Code to become prescriptive on the specific type of engagement and how it would be performed.

Technical Staff were pleased to note that Chartered Accountants Australia and New Zealand commented that they will assist their Members in understanding what the review should entail (refer to item 6 of the specific comments table). Technical Staff are also proposing to raise the matter with the AUASB as a potential consideration due to AUASB's pronouncement Guidance Statement GS 009 *Auditing Self-Managed Superannuation Funds*.

In addition to these changes above, Technical Staff also propose the following amendments:

- remove the option for a post-issuance review in proposed paragraph AUST R410.14.2, as a stakeholder noted that a pre-issuance review would be the most appropriate action to address threats in this situation. It also ensures that the review is being completed at the five-year mark rather than extending into the following year.
- Amend proposed paragraph AUST R410.14.2 to specify that the appropriate reviewer should not be involved in the Audit Engagements and should also be from another Office of the Firm.
- Delete proposed paragraph AUST 410.14.2 A1 as it was relevant for actions proposed in Options 2 and 3, which Technical Staff are not recommending for adoption.

Technical Staff seek the Board's views on the outcome of the re-exposure draft process and the resulting proposed revisions to the fee dependency on a referral source provisions.

Technical Staff also seek the Board's approval to issue the proposed amending standard and related Basis for Conclusions as set out at Agenda Items 11 (a) and 11(b), respectively.

### **Staff Recommendations**

Subject to the Board's review comments, the Board:

- (a) Determine the preferred options for revisions to the proposed fee dependency on a referral source provisions;
- (b) Approve the revisions in the Amending Standard *Amendments to Fee-related provisions of APES 110 Code of Ethics for Professional Accountants (including Independence Standards)*.

### **Materials Presented**

Agenda Item 11 (a)	Draft Amending Standard to Fees provisions in APES 110 (Marked-up from exposure drafts);
Agenda Item 11 (b)	Draft Basis for Conclusion;
Agenda Item 11 (c)	General Comments Table ED 01/22;
Agenda Item 11 (d)	Specific Comments Table ED 01/22;
Agenda Item 11 (e)	Attachment 1 – Specific Comments Table ED 01/22; and
Agenda Item 11 (f)	Regulators Comments Table – CONFIDENTIAL (distribution to Board Members only)

**Authors:** Channa Wijesinghe  
Jacinta Hanrahan  
Rachael Tiong

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