

International Ethics Standard Board
for Accountants
Mr Stavros Thomadakis
IESBA Chairman

Mr Ken Siong
IESBA technical advisor

Sent by email to
KenSiong@ethicsboard.org

Paris, Wednesday 10th June 2020

Ref: JB.CGE.GCA 20200099

RE: CNCC response to the Exposure Draft on the "Proposed revisions to the fee-related provisions of the Code".

Dear Stavros,
Dear Ken,

In submitting to the IESBA the comments of the CNCC on the Exposure draft on the "Proposed Revisions to the Fee-related Provisions of the Code", I unfortunately have to express the deep concerns of the French profession towards the general direction taken by IESBA in this ED and also in the ED on non-assurance services.

Firstly, we are strongly opposed to the introduction in the Code of any statement or provision that the audit client payer model *"creates a self-interest threat"*. This would imply, or at least send the message, that there is an inherent flaw in the model that all the rules and standards of the Code are trying to "repair". We do not believe that the auditor cannot be independent because he is paid by the client. On the contrary, the auditor is paid by the client to be independent. Why sending such a message when the IESBA itself indicates that it *"does not intend to suggest changes to the current business model for audit engagements, which would go beyond its mandate"* and that the audit client payer model is *"generally recognized and accepted by intended users of the financial statements"*. It would cast an inherent doubt on the independence of the auditor that is neither useful, nor helpful.

Secondly, we find that overall, the proposals tend to drift the Code away from being principles based (building on the risk and safeguard approach) by introducing new rules which bear the risk of discharging the auditors, and Those Charged with Governance, of their responsibilities. Ultimately it is for the auditor, and Those Charged with Governance, through an appropriate two-way communication, to judge whether proper safeguards have been put in place to preserve the independence of the auditor. Professional judgment must be exercised by both parties, in the specific circumstances of the engagement. We find that the role played by those charged with Governance in protecting the auditor's independence is not fully recognised and the exposure draft often introduces prohibitions or rules on issues which could have been dealt with by discussions with Those Charged with Governance and safeguards.

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Finally, we note that a lot of the issues highlighted in the exposure draft could be mitigated if the duration of the initial audit engagement was longer as it is the case in France where the duration of the initial audit engagement is six years. It provides a relief against the possible client's pressure not to renew the auditor's engagement from one year to the other.

You will find below our detailed answers to the questions of the exposure draft. Should you need any other information, please do not hesitate to contact us.

Best regards,


Jean Bouquot
President of CNCC

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)?**

The position of the IESBA, as stated in the explanatory memorandum to this ED, appears to be unclear, if not ambiguous, on this issue of the “audit client payer model”. In paragraph 22 of the explanatory memorandum to the ED, it is stated that *“the IESBA proposes that the Code should recognize the inherent self-interest threat in the audit client payer model”*, while in paragraph 25, it is mentioned *“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.”*

We do not support introducing into the Code the principle that *“When fees are negotiated with and paid by the audit client, this creates a self-interest threat [...]”* as stated in paragraph 410.4 A1.

It would cast an inherent doubt on the independence of the auditor for a practice that the IESBA itself recognizes as *“generally recognized and accepted by intended users of the financial statements”* (410.3 A1) after having also stated that *“the IESBA does not intend to suggest changes to the current business model for audit engagements”*. We therefore believe that it is neither useful, nor helpful to introduce such a statement in the Code.

We believe that one important element when dealing with this issue of the “audit client payer model” is the role of Those Charged with Governance vs Management of the client. The role of Those Charged with Governance (audit Committee in a PIE) should counterbalance the role of Management and the responsibility of the Audit committee to ensure the quality of audit should lead it to make sure that the auditor has the appropriate means and fees to conduct a high-quality audit. On the other hand, discussing and negotiating with the Management of the audit client is also very important for the auditor to be able to scope and price the audit since it is the Management of the audit client who has a detailed and an in-depth knowledge of the entity or the group and of its systems.

The question of the “audit client payer model” is therefore not that simple, as to be reduced to a statement that it “creates a self-interest threat”.

- 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?**

Yes, we support.

- 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?

We concur with the views expressed within IESBA that giving the example of Independent committee of the firm advising on Governance matter as a "safeguard" to the inherent self-interest risk of the "audit client payer model" would go beyond the remit of this project. It would even go beyond the mandate of the IESBA which role is not to issue guidance as to how the firms should be organized. ISQM is the standard which deals with how the firms should get organized to manage quality (including independence). If such an example was to be given it would be better placed in ISQM than in the IESBA Code.

But overall, we are not in favor of mandating or even recommending such independent committee. It would create a difference between the large firms and the smaller firms, because a small firm would never be able to have such an independent committee advising it on governance matter. It could lead to a severe reduction in the number of PIE audit firms, as we already see in certain countries where there are less than 10 PIE audit firms left, and ultimately to a further concentration of the market.

The existing Governance of the firms together with the Governance of the audit clients should be able to deal with issues of independence if and when they occur.

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?**

We believe that the level of audit fees must be sufficient to enable the auditor to perform a high quality audit irrespective of whether there are, or not, other services provided to the audit client; so that the audit can stand alone even if there are no other services provided to the audit client.

However, when it comes to the question of the firm's fee dependency from one audit client, it is necessary to consider both audit and non-audit services provided to that client.

Finally, we believe that there appears to be a certain contradiction between paragraphs 410.6 A1 and A2, where A1 seems to say that the provision of other services should not influence the determination of audit fees while A2 recognizes that the provision of other services can generate cost savings on the audit.

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?**

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Firstly, we note that it is the first time that the notion of the proportion of audit /non audit fees appears in the Code and that such guidance is not commanded by a requirement. It is therefore hanging.

Secondly, we consider that including all related entities is too wide. It should be limited to entities included in the scope of the consolidated financial statements. Services rendered to entities which are not in the scope of the consolidated financial statements could rarely threaten the independence of the auditor.

In the series of bullet points of paragraph 410.10 A2:

- we disagree with the fourth bullet point, the significance of the client to the firm. This is an issue of fee dependency of the firm towards an audit client, not of the ability of the auditor to issue an independent opinion on an audit client because of the large proportion of other services provided by the firm or the network to that client.
- We agree with the third bullet point, the nature of the services.

Building on that last point of the nature of the services, we believe that in fact there are two questions on the issue of the proportion of audit vs non-audit services fees for an audit client:

- The question of whether there is a proportion of non-audit services fees above which there is a self-interest threat to the auditor's objectivity that cannot be mitigated by safeguards
- The question of which services are part of the audit or related to the audit and which one are not. And amongst those that are not part or related to the audit which one are, because of their nature, creating a threat to the auditor's objectivity.

On the first question we do not believe that there is a proportion of non-audit fees above which the auditor's objectivity cannot be safeguarded. There can be a very significant acquisition one year on which the auditor provides acquisition due diligences services which fees represent twice the audit fees and nevertheless the auditor's objectivity is not impaired.

It is more the nature of the services provided which can cause a threat to objectivity. Audit related and other assurance services are by nature not creating a threat to objectivity. Services that create an advocacy threat are probably riskier.

Finally, we would like to highlight the fact that this entire question of the threat to the auditor's independence because of the provision of non-audit services is made more difficult where the audit engagement is short, especially in the case of a one-year audit engagement. In France we have a six year's audit engagement which constitute a very strong safeguard to the auditor's independence because it provides a relief against the possible client's pressure not to renew the auditor's engagement from one year to the other.

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?**

We agree with IESBA that the issue of fee dependency is important but we consider that it is properly dealt with in the extent Code. Therefore, we do not support the introduction of a threshold, especially for non-PIE audit clients, and we do not see what it brings to the issue, 30% is arbitrary and it is discriminatory to the smaller firms. The IESBA code is principle-based and should not set such kind of rules especially when they are so arbitrary.

We do not see any reason why the provisions of the extent Code should be changed regarding the fee dependency for non-PIE audit clients. The non-PIE audit market is still served by a number of SMPs and we believe that the introduction in the Code of the proposals in paragraph R410.14 would result in a greater concentration of the non-PIE audit market, which is not desirable.

We therefore recommend to revert to the extent provisions of the Code on that topic.

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?

We do not support the proposed actions in paragraph R 410.14 because we do not believe they are realistic. Regardless of the potential reluctance of the firm to let an external auditor review the audit opinion on one of their clients, the mere fact of finding an external independent reviewer, outside of the firm, may be very difficult for an SMP. Such persons are not easily identifiable, when they exist. And there is a risk that some auditors would specialize in rendering that service, becoming "professional" independent reviewers, losing their relevance overtime, or their independence if there are very few of them available on a small market.

However, we support the proposal in paragraph R410.16, that when the audit is conducted jointly by two or more firms, such joint-audit, with appropriate cross-review, constitutes a safeguard for the independence of the auditors.

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?

We do not support the proposed action in paragraph R 410.17 because we believe that the extent provisions of the Code regarding fee dependency for PIE audit clients are better suited to realistically address the topic.

Firstly, we believe that when the auditor is in a situation where the total fees from a PIE audit client are likely to represent for the second consecutive year more than 15% of the total fees received by the firm, the first step should be to go to Those Charged with Governance and discuss the matter with them, as required by paragraph R410.24.

Secondly, we do not understand why the present proposal has eluded the possibility of a post-opinion review which exist in the extent code and should be retained.

Thirdly, we believe that keeping the external "pre-issuance review" as the only possible safeguard is not practicable. The auditor will never be able to find an external independent reviewer, in the

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constraint deadlines in which the audit of the PIE clients, and especially of the listed clients, is conducted.

Finally, as in the case of the Non-PIE audits, we support the proposal in paragraph R410.18, that when the audit is conducted jointly by two or more firms, such joint-audit, with appropriate cross-review, constitutes a safeguard for the independence of the auditors

- 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?**

We do not support the introduction in the Code of this new proposal which sets an obligation to cease the engagement without offering any possible safeguard. It is excessive. Here again, the issue should be first discussed with those charged with Governance who are ultimately responsible to judge whether they are satisfied with the independence of the auditor.

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

Consistent with our response to question 9 above, we believe that it would be better that the firm consult first with the audit committee of the client to check that the audit committee is aware of the situation and is satisfied with the auditor's independence. And then, if the public interest dimension of the client is such that it is strategic or systemic to the economy, the auditor could consult an independent regulatory body or a professional body. But it should not be the case for all PIEs.

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?**

No, we do not believe that the disclosure of audit fees should be dealt with in the Code of Ethics. It is a matter of regulation, either of the Stock Exchange regulation, or of the accounting regulation or of the auditing regulation, but not for the Code of Ethics.

The principle should always be that the fees are disclosed by the client, not by the auditor.

We disagree with the requirement in R410.25 (a) (ii) that the firm shall be satisfied that the information is publicly disclosed about "actual or estimated fees paid or payable to other firms that have performed audit procedures on the engagement".

- Firstly, because we do not see how the auditor could check fees payable to other firms. The auditor can check fees payable to the firm and the network firms, but not to other firms.
- Secondly, because we do not see how fees paid to other firms can impact the auditor's independence.

Similarly, we do not support the requirement in paragraph R410.25 © to publicly disclose the fact that the total fees received by the firm from the audit client represent more than 15% of the total fees received by the firm. We do not see the relevance of that information to the Public. It will cast a doubt on the independence of the auditor without allowing the disclosure of the safeguards which

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have been put in place to ensure the auditor's independence and thereby give an incomplete information that may mislead the Public.

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?**

We believe that it is primarily to Those charged with Governance and specifically to the audit committee for the PIE audit clients, to confirm why they consider the auditor to be independent. They should do so to the shareholders who ultimately approve the financial statements in the General Assembly.

The auditor's independence is also confirmed to the public through the statement in the auditor's report that the auditor is independent.

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.

Some provisions of the proposed ED do not favor a free competition within the audit market and may lead to greater concentration on both the PIE and Non-PIE audit market.

This is the case of the restrictions on the size of audit clients entailed by the fee dependency provisions in the ED which are much more stringent than the extent and which do not leave much opportunity for a medium sized firm to grow in both size and experience with larger clients.

This is also the case when the ED requires the disclosure of the fees paid to other firms or when it requires the public disclosure of the fee dependency of the firm towards the audit client.

Such provisions will disqualify some firms of the audit market, when they are in fact perfectly independent and objective in issuing their opinion.

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?

To the extent that we do not support a certain number of proposals from the ED, we do not support the consequential amendments they would entail on the other assurance services section.

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?

No.