



National Association of State Boards of Accountancy

◆ 150 Fourth Avenue, North ◆ Suite 700 ◆ Nashville, TN 37219-2417 ◆ Tel 615.880-4201 ◆ Fax 615.880.4291 ◆ www.nasba.org ◆

February 22, 2018

International Ethics Standards Board for Accountants (IESBA)

529 Fifth Avenue
New York, NY 10017

Via email: GeoffKwan@ethicsboard.org

Re: Fee Questionnaire

Dear Members of the IESBA:

The National Association of State Boards of Accountancy (NASBA) appreciates the opportunity to respond to the above referenced Fee Questionnaire (the Questionnaire). NASBA's mission is to enhance the effectiveness and advance the common interests of State Boards of Accountancy (state boards) that regulate all Certified Public Accountants (CPAs) and their firms in the United States and its territories which includes all audit, attest and other services provided by CPAs. State boards are charged by law with protecting the public.

In furtherance of that objective, NASBA offers the following responses to the questions raised in Section B.4, Regulators and Audit Oversight Authorities, of the Questionnaire.

Responses to the Specific Questions Raised in the Questionnaire

General

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

NASBA believes that the level of fees charged by an audit firm could give rise to ethics and/or independence issues in some circumstances. Whether fees associated with an attest engagement are unusually large or small is not, by itself, an ethics violation. However, such conditions may introduce threats that elevate the risk of unethical behavior.

Threats may result when, for example:

- Fees are too low to reasonably perform an engagement and comply with standards
- A firm, office, or partner is financially dependent on an individual client
- Fees from an individual client represent a significant percentage of total firm revenues or drive a significant percentage of an engagement partner's compensation.

The public would expect that most accountants do not intend to lose money in performing services absent an overall business strategy to make themselves whole. Some steps may be acceptable, however they must not present potential threats to ethical conduct. For example, when an auditor charges a low fee, the auditor might subordinate his/her judgement on certain matters rather than devote additional time to investigate an audit issue. While this situation involves an element of failure to exercise due care, it could also result in the auditor's failure to act with integrity, objectivity and, arguably, independence. Sometimes, auditors may decide to "invest in a client," try to build a practice in a certain industry or area, or perform charitable work and, consequently, will perform an audit at a loss. However, if the auditor is aiming to please the client in hopes of getting additional work, e.g., from the client or a board member, the auditor may not have an independent mental attitude.

Another potential threat to ethical behavior exists when fees from a particular client or group of related clients are significant to a firm's revenues, or to certain offices or partners in the firm. The type of issues and the magnitude of the impact from these threats likely will differ for a large multinational firm compared to a smaller firm. In the case of a larger firm with multiple offices and partners, for example, the total fees charged on a single engagement are unlikely to be material to the overall revenues of the firm. However, a threat may exist when the fees from a client represent a significant proportion of the revenue in a large firm partner's book of business or proportion of the revenue of an office of the firm. On the other hand, for a smaller audit firm, if the total fees charged to a single audit client are a sizable portion of the total firm revenues, the dependence on a client and concern about losing the work could create self-interest and/or intimidation threats to independence, integrity and objectivity.

2. *Has your organization identified from inspections, disciplinary investigations or other means, any fee-related issues that might have created threats to compliance with the fundamental principles or to independence? If so, please describe the finding. For example:*
 - *What was the nature of the issue?*
 - *How frequently did it occur and what was the severity?*
 - *Did the firm appropriately deal with the issue? If not, do you believe that there are impediments that might have affected the firm's response, and if so, what were they?*

Though fees were not the primary issue, at least one state board addressed audit failures of program-specific audits performed in accordance with U.S. Department of Housing and Urban Development (HUD) requirements and observed that below market fees were a significant and consistent factor that may have impacted the auditor's ability to provide a quality audit in a timely manner.

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

NASBA is not aware of other concerns about the level of fees charged for audit or non-audit services.

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

NASBA believes that the provisions of the IESBA Code are generally adequate; however, we do suggest the IESBA consider further safeguards for smaller firms.

NASBA also believes that standards of ethical conduct should not be fee-driven or prescriptive; however, fee issues should be considered in the IESBA Code.

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

Yes, in two states of the United States, Mississippi and Texas accountancy board rules and statutes, respectively, are more stringent than provisions in the IESBA Code. Specifically, independence is presumed to be impaired when a CPA performs audit services for a fee that is less than the direct labor costs of the engagement. Below are the excerpts from the appropriate rule and statute of the respective states:

Mississippi State Board of Public Accountancy:

Rule 6.2.3. Independence will be presumed to be impaired if the CPA or firm permit holder performs audit services, other than for charitable organizations, for a fee that is less than the direct labor cost reasonably expected at the time the engagement was accepted to be incurred in performing such services. For this purpose direct labor costs means the total compensation of the person or persons expected to perform the service for the time they are expected to serve on the engagement plus all payroll expenses related to such compensation.”

Texas State Board of Public Accountancy:

Tex. OCC. Code Sec. 901.458. LOSS OF INDEPENDENCE.

(a) In this section, "direct labor cost" means:

- (1) the total compensation paid to a person who performs services; and
- (2) the employer payroll expenses related to that compensation, including workers' compensation insurance premiums, social security contributions, costs of participating in retirement plans, group insurance costs, and unemployment taxes.

(b) A person creates a presumption of loss of independence if the person:

- (1) holds a certificate or firm license issued under this chapter; and
- (2) performs or offers to perform an attest service for compensation that is less than the direct labor cost reasonably expected to be incurred in performing the service...”

(c) This section does not apply to the donation of services to a charitable organization as defined by board rule.

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

Although NASBA is not aware of significant current issues, in the past state boards have raised the following concerns:

- Fees are too low to reasonably perform an engagement and comply with standards
- A firm, office, or partner is financially dependent on an individual client.

When practitioners identify threats to fundamental principles, NASBA believes that practitioners should determine whether appropriate safeguards are available to eliminate or reduce the threat to an acceptable level. Among other things, such safeguards may include:

- Institute adequate systems of quality control, including acceptance and continuance of engagements
- Require adequate supervision and review of engagements
- Allocate a reasonable amount of time to complete the engagement
- Assign qualified staff to the engagement team
- Participate in quality reviews, e.g. concurring or second partner reviews
- Consult with technical specialists on issues involving significant judgement
- Discuss relevant risks and applied safeguards with the client’s governance body.

NASBA suggests that IESBA re-evaluate the safeguards described in the Code to determine whether they adequately address fee issues. NASBA also suggests that IESBA work with members of the Small and Medium Practices Committee to develop further guidance on the implementation of safeguards for smaller firms addressing these type of fee issues.

Non-Audit Services

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

As noted in our response to Question 5, regulatory provisions in two states in the United States address the loss of independence posed by audit services performed for less than direct labor costs. These states generally adopt an approach to this issue that is based on AICPA standards and interpretations of these standards, specifically, AICPA ET Section 100 - Conceptual Framework for AICPA Independence Standards. It should be also noted that the vast majority of US state accountancy acts/board of accountancy rules require CPAs to follow the AICPA Code of Professional Conduct; therefore, this independence framework is relevant to most US states.

The approach set forth in AICPA ET Section 100 - Conceptual Framework for AICPA Independence Standards is directly patterned after independence standards developed by the International Ethics Standards Board of Accountants.

NASBA is not aware of specific regulatory provisions that apply to the level of fees charged for non-audit services provided to audit and assurance clients.

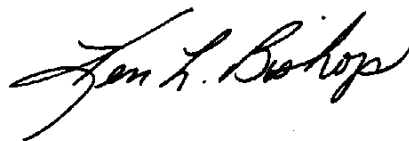
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We appreciate the opportunity to respond to the Questionnaire.

Very truly yours,



Theodore W. Long, Jr., CPA
NASBA Chair



Ken L. Bishop
NASBA President and CEO