



**Consultation on a model for the apportionment of a levy on  
auditors of Public Interest Entities**

## **Table of Contents**

1)	Introduction .....	1
2)	Overview of AIU levy .....	1
3)	Costs to be levied .....	1
4)	Mechanism for levy collection .....	2
5)	Summary of possible allocation methods .....	2
6)	Flat rate levy .....	3
7)	Pro rata levy.....	3
8)	Cost per inspection .....	5
9)	Two tier levy.....	5
10)	Questions on which IAASA is consulting .....	5
11)	Making your submission .....	6
	Appendix 1 – Section 918 of the Companies Act 2014 .....	7
	Appendix 2 - Summary of 2014 Funding models of other audit regulators .....	8

## 1) Introduction

As part of the recent European audit reform measures, including in particular Regulation 537/2014, with effect from June 2016 IAASA will assume responsibility for inspecting the quality of audit work performed by the auditors of Public Interest Entities ('PIEs'). As a result, IAASA is currently establishing an Audit Inspections Unit ('AIU'). The AIU's overall objective will be to implement Regulation 537/2014, to inspect PIE auditors' work and to promote improvements in the quality of auditing of PIEs.

Section 918 of the Companies Act 2014 provides that IAASA may impose, with the Minister of Jobs, Enterprise and Innovation's ('the Minister') consent, one or more levies on the auditors of PIEs (the 'Firms') in order to fund the costs of the AIU. In particular, section 918(5) provides that IAASA shall establish criteria for apportioning the levy among the Firms and section 918(6) anticipates that different Firms may be required to pay different amounts.

In this context, it is anticipated that IAASA will levy the costs of the AIU on the Firms with effect from June 2016.

For ease of reference, the text of Section 918 is set out in Appendix 1 and the text of Regulation 537/2014 may be accessed [here](#).

## 2) Overview of AIU levy

As noted above, IAASA is mandated by section 918(5) of the Companies Act 2015 to establish criteria for apportioning the AIU levy among the Firms. When considering possible apportionment models, IAASA liaised with a number of our international counterparts, currently inspecting PIE audit firms, regarding their respective funding models. A table summarising our understanding of such funding models is set out in Appendix 2.

The next phase of IAASA's consideration of this matter is this public consultation from which we hope to obtain wider views from stakeholders and other interested parties. Some of the principles which IAASA will have in mind when finalising the proposed apportionment model for the AIU levy include:

- The allocation of AIU costs among the Firms should be proportionate to the time and effort required to inspect the relevant Firms;
- The apportionment model adopted should be objective and transparent;
- The model should be based on easily identifiable and verifiable information that does not impose an unnecessary administrative burden on either IAASA or the Firms;
- The model should be cost effective and provide a stable basis for IAASA to raise the funds required to carry out our statutory duties;
- Not setting the proposed criteria for the apportionment of the levy at a level which makes entry to the PIE audit market unaffordable for new entrants; and
- Ensuring that the method for calculating the apportionment of the levy is clear, and limits any ambiguity or potential for misinterpretation.

## 3) Costs to be levied

The costs of the AIU which may be levied on the Firms fall into four categories, as detailed below.

- *Direct / core operating activities, including inspection costs*

These will include directly attributable costs such as:

- Staff salaries and related costs;
- Travel and subsistence;
- Portable ICT assets;

- Training;
- Legal advice; and
- Experts' and consultant's fees.
- *Overhead costs*  
Overhead costs will include the AIU's relevant share of overhead costs based on headcount such as:
  - Premises;
  - Lighting;
  - Heating;
  - ICT support;
  - Administrative expenses; and
  - Insurance.
- *Investigation and disciplinary costs – standing costs*  
The standing costs of the investigation / conduct part of the AIU work will be included in the amount to be levied on the Firms.
- *Investigation and disciplinary costs – case specific costs*  
It is envisaged that a dedicated and significant reserve fund will need to be established to fund IAASA's PIE investigation and disciplinary work. This will allow the AIU to have the resources to quickly respond to unanticipated developments, such as investigations. Funding would be raised through the levy and also from fines and costs arising as a result of settlements, preliminary investigations and Inquiries. This concept will be explored further as the Department of Jobs, Enterprise and Innovation develops the legislation enacting the European audit reform measures in the coming months.

#### **4) Mechanism for levy collection**

The amount to be levied will be based on the relevant portion of IAASA's programme of expenditure for the year and will be invoiced to the Firms on a quarterly basis. Any timing differences arising at the year end between the aggregate of levies received from the Firms and IAASA's net relevant expenditure in the year will be reflected as debtors or levy income carried forward. Such balances will be taken into account in invoicing the following year's levy. Where the programme of expenditure is not sufficient for the year, a supplementary programme of expenditure will be approved by the IAASA Board and submitted to the Minister for consideration. Subject to Ministerial approval, a supplementary amount will be levied on the Firms.

#### **5) Summary of possible allocation methods**

The following possible allocation options have been considered and included in this consultation paper:

- Flat rate levy (section 6 below refers);
- Pro rata levy based on one, or more, of the following:
  - Number of PIE audit clients, i.e. a flat rate per client (section 7.1 below refers);
  - Number of PIE audit clients, with provision for PIE size/types (section 7.2 below refers); and/or
  - Fee income from PIE audits (section 7.3 below refers);
- Cost per inspection (section 8 below refers); or

- Two tier levy (section 9 below refers).

A number of other possible allocation options were considered and excluded from this consultation paper due to a number of reasons including complexity, availability of accurate information, potential for ambiguity and inconsistency and lack of proportionality. Such options included:

- Pro rata levy based on the number of statutory auditors employed;
- Pro rata levy based a Firms' number of offices; and
- Pro rata levy based on the number of total audit hours related to PIE clients.

## 6) Flat rate levy

Under a flat rate levy each Firm would pay an equal amount.

### Advantages

- Simple to calculate and administer.
- Transparent.
- This model could be considered to be equitable in the sense that all Firms contribute equally.

### Disadvantages

- This may be regarded as inequitable as smaller Firms would be required to contribute to the same extent as the large Firms, despite having significantly less PIE audit clients and, potentially, less frequent AIU visits.
- This model does not have regard to the varying levels of complexity of different categories and sizes of PIEs and, consequently, to the varying time commitment required by the AIU to perform reviews of various categories of Firms' PIE audit files.
- The high cost per Firm may be viewed as a barrier to new entrants to the PIE audit market.

## 7) Pro rata levy

Using a *pro rata* levy, each Firm's contribution would be a function of their relative scale *vis-a-vis* the other Firms. A number of possible pro rata apportionment models are set out below.

### 7.1. Number of PIE audit clients (flat rate per client)

Using this model, each Firm would be charged according to the number of PIEs it is responsible for auditing.

#### Advantages:

- Easy to calculate and administer.
- The Firms are required to provide details of their PIE audit clients in their Annual Transparency reports and this information can easily be verified.
- This levy model could be considered an equitable approach as it is directly proportionate to the number of PIEs audited by each Firm.

#### Disadvantages:

- This levy model may be regarded as inequitable as it does not incorporate a weighting for equity PIEs and the large financial institutions which would be perceived as higher risk than other categories of PIEs, and hence would be expected to require proportionately more AIU time.
- An inspection of "whole firm" procedures (as opposed to audit engagement inspections) will need to be completed for each Firm, regardless of the number of PIE

clients. However, the costs allocated to the smaller Firms may be disproportionately low under this method to take account the cost of performing this part of the inspections.

## **7.2. Number of PIE audit clients, with provision for PIE size / type**

Under this model, while each Firm would be charged based on the number of PIE audit clients as in section 7.1 above, the charge per PIE audit client would be based on the relative size or type of client concerned. Possible models include:

- Allocation based on categories of PIEs (different charge for equity, financial and insurance entities); or
- Allocation using a financial measure to determine the relative size of each PIE (turnover, profit/loss, total assets, market capitalisation etc).

### Advantages:

- Equitable as, in addition to being proportionate to the number of PIE audit clients per Firm, such an approach attempts to reflect the relative size and complexity of different PIEs.

### Disadvantages:

- May be administratively complex, depending on the method selected.
- Firms may not have the data required readily available to support the method selected.
- Time consuming to verify information provided by the Firms if a financial measure is chosen.
- May be difficult to ensure consistency of information provided by Firms. Clients have different year ends, reporting currencies etc.
- Measures such as market capitalisation, total assets and revenue do not necessarily reflect the complexity of the relevant PIEs' financial reporting.
- Whereas market capitalisation and/or revenue data is readily available for equity PIEs, such indicators tend not to be relevant in the case of funds and debt PIEs, where total investments/debt in issue may be a more relevant measure. Accordingly, such an approach would give rise to difficulties associated with the comparability of data.
- An inspection of "whole firm" procedures (as opposed to audit engagement inspections) will need to be completed for each Firm, regardless of the number of PIE clients. However, the costs allocated to the smaller Firms may be disproportionately low under this method to take account the cost of performing this part of the inspections.

## **7.3. Fee income from PIE audits**

Each Firm would be levied according to its audit fee income from PIE clients.

### Advantages

- Equitable as fee income should be reflective of the size and complexity, and therefore the potential risk, of the PIEs subject to audit by each Firm.
- Firms will be required to provide this information under Regulation 537/2014.

### Disadvantages

- Information controlled by each Firm and is not readily verifiable.
- Extra administrative burden for IAASA to ensure that the Firms' reporting of audit income per client is accurate, particularly where a PIE is part of a group.

## 8) Cost per inspection

Under this method, the Firms would be charged based on the cost of each inspection incurred by the AIU.

### Advantages

- May be viewed as the most equitable allocation method as all Firms would contribute according to the time commitment required by the AIU to complete each review.

### Disadvantages

- May be difficult to calculate, particularly on commencement of the AIU regime, where it may be challenging to accurately forecast the amount of time to be spent at each Firm.
- Firms would be subject to a significant charge in the years that they are subject to inspection and none in other years.
- May be difficult to ensure a consistent funding stream for the AIU's overheads and indirect costs.

## 9) Two tier levy

Under this allocation method, each Firm's levy would be a combination of:

1. A standard or minimum charge; and
2. A pro rata charge, using one of the methods outlined in section 7 above, or a charge per inspection, as outlined in section 8 above.

### Advantages:

- Combines the simplicity of a flat rate levy, with the perceived equity of a pro rata allocation method.
- Reflects both the time and effort of the AIU in inspecting the Firms and the PIE clients and their profile.

### Disadvantages:

- More complicated to calculate than a single pro rata or flat rate levy, although this could be mitigated through the use of a minimum levy.

## 10) Questions on which IAASA is consulting

In light of the above, a number of questions are set out below on which we would welcome views from stakeholders and interested parties.

- a) Please indicate your favoured levy model, of those outlined in sections 6 to 9 above, for use by IAASA in levying the costs of the AIU on the Firms and specify your reasons for this choice.
- b) Are there any further advantages or disadvantages to any of the models outlined in this paper that you believe should be considered by IAASA when selecting a levy model?
- c) Do you think that another method not outlined in this paper should be considered as the funding model for the AIU? If so, please outline this model and specify your reasons for its use.
- d) Do you think that there should be a minimum charge levied on each Firm? Please provide reasons for your answer.
- e) Do you think that the costs set out in section 3 above fairly reflect the types of costs which should be levied on the Firms? If not, please a) note what costs you think should be excluded and a proposed alternative mechanism for funding such costs; and b) set out the nature of any additional costs you think should be further included and the reasons for same.

- f) Do you agree that the specific case costs of investigation and discipline should be shared in accordance with the apportionment model across all Firms or should the individual Firm being investigated pay the specific costs of such a case? Please provide reasons for your answer.
- g) Please provide any additional comments you may have on the proposals set out in this consultation paper.

## 11) Making your submission

Please provide responses to the above questions by e-mail only to [submissions@iaasa.ie](mailto:submissions@iaasa.ie) no later than **midnight on 6 November 2015**. Any submissions received after this date or any anonymous submissions will not be considered.

IAASA invites comments on all proposals put forward in this paper and in particular on the specific questions summarised in section 10 above.

Comments are most helpful if they:

- Respond to the question stated;
- Indicate the specific point to which a comment relates;
- Contain a clear rationale;
- Provide evidence to support the views expressed/rationale proposed; and
- Describe any alternative levy option(s) you wish IAASA to consider.

While responses may include attachments, such attachments must not be encrypted. All responses received by the deadline will be considered prior to IAASA's submission to the Minister.

Depending on the nature and scale of responses, IAASA may publish a feedback statement summarising the content of the responses. Respondents should note that, in the interests of transparency, their responses may be published in full or in part (and may be attributed to the respondent) by IAASA in that feedback statement.



## **Appendix 1 – Section 918 of the Companies Act 2014**

### **Funding in respect of functions of Supervisory Authority under certain regulations**

- (1) In this section “public-interest entities” has the same meaning as in Regulation 3 of the 2010 Audits Regulations.
- (2) For the purposes specified in subsection (3), the Supervisory Authority may impose, with the Minister’s consent and subject to subsections (4) to (6), one or more levies in each financial year of the Supervisory Authority on statutory auditors and audit firms auditing public-interest entities.
- (3) Money received by the Supervisory Authority under this section may be used only for the purposes of meeting expenses properly incurred by it in performing its functions under Regulations 83 and 84 of the 2010 Audits Regulations and under any other Regulations of those Regulations that contain consequential or incidental provisions on, or in relation to, those Regulations 83 and 84.
- (4) In addition to the requirement under subsection (2) with regard to the Minister’s consent, the total amount levied in any financial year of the Supervisory Authority on statutory auditors and audit firms shall not exceed an amount in relation to that year specified in writing by the Minister for the purposes of this subsection.
- (5) The Supervisory Authority shall—
  - (a) establish criteria for apportioning a levy among the several statutory auditors and audit firms auditing public-interest entities,
  - (b) submit the criteria to the Minister for approval before imposing the levy, and
  - (c) specify the date on which the levy is due to be paid by the relevant statutory auditors and audit firms.
- (6) As a consequence of the apportionment of the levy under subsection (5), different statutory auditors and audit firms may be required to pay different amounts of the levy.
- (7) Notwithstanding that the particular audit of a public-interest entity has been carried out by a statutory auditor, no levy under this section shall be imposed on the statutory auditor if he or she was designated by a statutory audit firm to carry out the audit, and the levy under this section shall, in those circumstances, be imposed on the statutory audit firm instead.
- (8) The Supervisory Authority may recover, as a simple contract debt in any court of competent jurisdiction, from a statutory auditor or audit firm from which the levy is due, a levy imposed under this section.

## Appendix 2 - Summary of 2014 Funding models of other audit regulators

Country	Levy charged to audit firms to cover inspection costs	Single or multiple tier levy?
UK (FRC)	No direct levy on the audit firms. Rather, direct variable costs are levied on the professional bodies with which the relevant auditors are registered.	Single
Luxembourg (CSSF)	Charge based on the number of statutory audit assignments, which also includes non-PIEs (from €1k for under 10 clients to €500k for over 3,500 clients).	Single
Denmark (DBA)	Actual cost per inspection charged to each PIE auditor.	Single
Netherlands (AFM)	Basic fee of €1,500 plus levy based on audit revenue (applies to both PIE and non-PIE auditors).	Two tier
Italy (CONSOB)	Levy on statutory auditors based on a percentage of revenues from statutory audits of PIEs (8.85% in 2014).	Single
Finland (AB3C)	Levy per audit client based on the market value of their publicly traded securities or the value of equity per their financial statements if the securities are not publicly traded.	Single
USA (PCAOB)	No direct levy on the audit firms. Rather, there is a charge on issuers, based on their average monthly U.S. equity market capitalisation or net asset value.	Single
Switzerland (FAOA)	Annual oversight levy based on audit fees, subject to a minimum charge of CHF 10,000 (approx €9,230), and an 'inspection fee' based on a daily rate per inspector of CHF 1,000 to CHF 2,500 (approx €923 to €2,307).	Two tier
Sweden (RN)	Based on the number and size of PIEs audited by an individual audit firm, ranging from 40,000SEK (approximately € 4,500) for a large PIE to 10,000SEK (approximately € 1,150) for a small PIE.	Single
Canada (CPAB)	Based on a percentage of audit fees, collected via the audit firms, but the charge is on the issuers.	Single
Germany (APAK)	Two tier levy comprised of a standard charge of €1,900 per PIE audit client and 0.51% of PIE audit fees.	Two tier
France (H3C)	Funding is based on: <ul style="list-style-type: none"> <li>• A fixed annual fee of €10 per statutory auditor;</li> <li>• A fixed fee for each audit opinion issued (from €20 to €1,000 for listed entities); and</li> <li>• A levy of between 0.65% and 1% of overall PIE audit fees in the previous year.)</li> </ul> All charges are collected by the professional body for auditors in France.	Three tier