Auditors' Fees, smaller companies (UK & Ireland)

Background and Overview

Over a number of years, investors have increasingly raised concerns that non-audit services provided by the auditor of a company may impair audit objectivity. As a result, many investors do not support proposals authorising the board to fix the fees payable to the external auditors when auditors received significant non-audit fees and there is no satisfactory explanation for the provision of the non-audit services by the auditor.

ISS UK and Ireland policy generally considers non-audit fees to be excessive when they routinely exceed audit-related fees without adequate explanation, and will recommend voting against proposals relating to auditor fees when the ratio of non-audit fees to audit fees has been over 100% for more than one year without adequate explanation. This is applied to widely held companies (generally the main index companies in UK and Ireland). It is not currently applied to smaller companies (defined here as those companies which are members of the FTSE Fledgling index, those listed on AIM and other companies which are not widely held).

Key Changes Under Consideration

ISS proposes to extend the current ISS UK and Ireland policy regarding fees for non-audit services, to be applied to smaller companies.

ISS would recommend a vote against proposals authorising the board to fix the fees payable to the external auditors when the ratio of non-audit fees to audit fees has been over 100 per cent for more than one year, there is no satisfactory justification (for example, exceptional circumstances linked to a one-off transaction) and the company appears unwilling to address the issue. In addition, the chairman of the audit committee may receive a negative voting recommendation when he or she is next standing for re-election.

Intent and Impact

The proposed change is intended to ensure that the policy for smaller companies in this important area is appropriately robust. It is designed to provide explicit guidance on the implications in cases where the size of the non-audit services could potentially impair the external auditor's objectivity, given the increasing scrutiny and restriction on non-audit services from both regulators and the investor community. The proposal also reflects comments and feedback received from investors.

The impact of this proposed policy is expected to be fairly limited. Based on a recent review of prior-year data, just under 6% of companies identified as smaller companies covered by ISS could be expected to be impacted in future years.

Request for Comment

1. Does your organization agree that a non-audit fee cap of 100% of the audit fee is appropriate for smaller companies? If not, please explain.
2. Does your organization consider that exceptions to the policy should be made in cases where the total fees payable to the external auditor are small? If yes, what would you consider an appropriate *de minimis* threshold to apply?