

RECOMMENDED PRACTICE GUIDE (RPG) 7

FEEES AND COMMISSION

PREFACE

This preface has been approved by the Council of the Malaysian Institute of Accountants (MIA) in January 2007 for publication.

INTRODUCTION

The recommended practice guide (RPG) contained herein have been developed in response to enquiries received and changing circumstances in which the accountants functions in.

It represents best current practice endorsed by the Institute.

In developing this practice guide, the Malaysian Institute of Accountants (MIA) had conducted the following due process:

- Determining the issues
- Research into current practice
- Consultation with various stakeholders
- Consultation with relevant regulatory authorities, where appropriate
- Recommendation by the Public Practice Committee of the MIA to Council for issuance as a RPG

APPLICABILITY

This RPG is a statement issued by the Council of the MIA. As such it constitutes part of generally accepted best practice in Malaysia and is therefore recommended that members apply the RPG in the performance of their respective duties.

In determining the acts of members in the performance of their respective duties, the Council may inquire into apparent failure by members to adopt this RPG.

EFFECTIVE DATE

This RPG is effective for members to observe from the date of issuance and is set herein as 1 January 2007.

RECOMMENDED PRACTICE GUIDE (RPG) 7 : FEES AND COMMISSION

1. Professional fees charged by members in public practice shall be a fair reflection of the value of the work performed for the client, and shall take into account inter alia –
 - (a) the skill and knowledge required for the type of work involved;
 - (b) the level of training and experience of the persons necessarily engaged on the work;
 - (c) the time necessarily occupied by each person engaged on the work; and
 - (d) the degree of responsibility and urgency that the work entails.

Explanatory Note:

- (i) In order to carry out the professional service for which he is engaged, a member in public practice must first consider the instructions of his client in conjunction with any statutory duty relating thereto and then discharge his responsibility by applying to the affairs of his client the professional skill and knowledge which he and his staff have acquired through training and experience.
 - (ii) The member's fees for that service should provide him with appropriate remuneration for the time and skill which he has personally devoted to his client's affairs and the responsibility he has accepted together with reimbursement of and a suitable margin of profit on his overhead expenses and the salaries of his staff for whose work he takes responsibility.
 - (iii) Fees should therefore normally be computed by reference to the above factors (a) to (d).
 - (iv) It is neither usual nor necessary for bills submitted to clients to be fully detailed but the member's records should be adequate to enable this to be done if required either to satisfy the client or in the unfortunate event of it becoming necessary to take legal proceedings to recover unpaid fees.
 - (v) For further guidance, please refer to Section 240, Part 1 of the By-Laws for Professional Ethics.
2.
 - (1) No member shall charge an unrealistic professional fee.
 - (2) In this respect, a professional fee of less than Ringgit Malaysia Five Hundred (RM500.00) for audit services shall be considered as an unrealistically low professional fee.
 - (3) Notwithstanding Para 2(1) and 2(2) of the above, a member may charge charitable bodies and non-profit organisations low professional fees or provide free services provided always that the provision of such services is not used as an inducement to secure professional appointments or engagements which may arise there from.
3.
 - (1) In specific circumstances where a member in public practice feels there are genuine grounds to propose a lower fee than another member undertaking the same or similar work (other than non-recurring or specialist work including management consultancy services), the member shall exercise due care to ensure that the lower fee is in line with the provisions of Para 1 above.

- (2) Subject to Para 3(1) above, any fee proposal of less than 90% of the fee previously charged shall be taken as prima facie evidence of a likelihood that a compromise or lowering of professional standards will result in the carrying out of the assignment.

Explanatory Note:

- (i) The fact that one member may charge a lower fee than another for undertaking the same or similar work is not improper provided due care is taken to ensure that the client is not misled:
 - (a) as to the precise range of services that a quoted fee is intended to cover (in which connection that member should provide the client with an engagement letter); and
 - (b) as to the likely level of future fees for any work undertaken for the client.
 - (c) that the member intending to charge a lower fee shall inform the client in the engagement letter referred to in sub-paragraph (i)(a) above of the precise range of services covered by the quoted fee.
4. (1) Fees shall not be charged and/or instructions shall not be accepted, on a percentage or contingency fee basis save where that course is authorised by statute or is generally accepted practice for certain professional services.
- (2) For further guidance, please refer to Section 240.3 and 240.4, Part 1 of the By-Laws for Professional Ethics which deals with the evaluation of threat and the implementation of safeguards where appropriate.

For further guidance, please refer to Section 240 in the By-Laws

5. (1) A member in public practice shall not directly or indirectly allow or agree to allow the participation by any person other than another member in public practice in the fees of his professional work.

Explanatory Note:

This Para does not prohibit members to undertake a project with other professionals of different competency where bills are issued on an aggregated basis and where there are actual justifications of the involvement of the other professionals in the said project.

- (2) The prohibition in Para 5(1) above shall not apply to any member paying or agreeing to pay any sum out of his profits or any remuneration to any retiring partner of the member's practice or of any related practice or to the personal representatives or the spouse or dependants of any deceased partner whether such partner had retired from practice or not at the date of his demise or to any predecessor in the member's practice or the personal representatives of such predecessor.
6. A member in determining audit fees shall take into consideration the Recommended Basis for Determining Audit Fees as set out as appendices to this RPG, which shall be applicable **in respect of all statutory audits.**

7. Any member in public practice who fails to comply with the provisions of this RPG shall be deemed to have compromised or lowered professional standards in carrying out his professional work, and this shall represent a valid reason for a complaint to be made against him.

8. (1) A member in public practice shall not -
 - (a) pay a commission to obtain a client;
 - (b) accept a commission for the referral of a client to another member or to a third party; or
 - (c) accept a commission for the referral of the products or service of others;

where such payment or acceptance would impair or give the appearance of impairing the objectivity, integrity or independence of the member in carrying out his professional work.
- (2) For further guidance, please refer to Section 240.7, Part 1 of the By-Laws for Professional Ethics which deals with the implementation of safeguards where appropriate.
- (3) The provisions in Para 8(1) above shall not prohibit payments for the purchase of an accounting practice or retirement payments to individuals formerly engaged in public practice or payments to their heirs or estate.

9. Payment and receipt of referral fees between members in public practice when no services are performed by the referring party shall be regarded as commission for the purpose of Para 8 above.

RECOMMENDED BASIS FOR DETERMINING AUDIT FEES

FOREWORD

Audit Fees shall generally be based upon the degree of responsibilities, risk and skill involved and the time necessarily occupied on the work by the partner and staff in terms of the quality and level of competence required to meet auditing standards and statutory compliance with reference to the size, complexity and technical input expected of the audit assignment.

The cost of time occupied, the time charge, will be based on the cost of the practice which shall include attributable direct cost, the recovery of overheads and the appropriate return on the investment in the practice (see Appendix I).

The time charge based on the aforementioned factors may vary from practice to practice. However, empirical studies carried out by the Institute way back in 1992 have shown a proportionate correlation between audit fees charged, based on time charge, and the value of total assets or gross turnover or operating expenditure (see Appendix II).

The value of total assets or gross turnover or operating expenditure is a fair reflection of the size and level of transactions of an entity. Therefore, as a benchmark to assist member firms in determining audit fees and also for the information of users of auditing services, subject to the Act and the By-Laws (on Professional Conduct and Ethics), where relevant, the Council recommends that appropriate audit fees level should be determined in accordance with the Appendices set out herein.

Appendix I

Audit Charge-Out Rates

(A) Introduction:

Time management is essential in ensuring efficiency in audit performance while time recording is an integral part of the documentary evidence of work performed.

Time charge shall be reflective of time spent by the partner and staff in terms of the quality and level of competence required to meet the auditing standards with reference to the size, complexity and technical input expected of the audit assignments.

A critical factor in maintaining the viability of a practice depends on good costing.

The determination of chargeout rate is costing for audit practice.

In the absence of a uniform basis, charge-out rates may differ due to inadequate or over computation of the variable cost factors.

The Council therefore recommends the basis for time charging as set out below. From past experience, cost computation based on the recommended basis will normally produce a factor of about three times the direct labour cost.

(B) Definitions

- (i) "Economic time charge" shall include the following :

Labour Cost
Opportunity Cost, equivalent to the direct labour recovery cost of each staff
Appropriate Recovery of Overheads
Profit Element

- (ii) The unit rate should be based on net working hours.

Net working hours:

Total chargeable hours based on the normal working days in the year of a practice net of annual holidays, annual leave, study and examination leave and firm's holidays.

- (iii) Total Labour Cost :

Actual Wage, including EPF and Socso Contribution
Training Cost, including course and examination fees
Cost of Study Leave
Gratuities
Welfare Cost

- (iv) Overheads Recovery Rate:

Members may wish to adopt the absorption method which will take into account the total net working hours of the practice. However, it may not be appropriate because the recoverability rate of each member of staff differs. An alternative is to derive the weighted average based on estimated administrative time of each grade of staff. The administrative time of each staff can be determined with reasonable accuracy from the time sheets submitted by each staff over a control period.

(C) Basis

Charge-out Rates shall be computed on the basis of economic time charge and should reflect its recoverability. It should include direct cost and also an appropriate proportion of fixed overheads.

(D) Calculation of Charge-out Rate

		RM
Direct Labour Recovery Rate represented by	<u>Total Labour Cost</u>	XX
	Net Working Hours	
Add		
Opportunity cost (represented by Direct Labour Recovery Rate*)		XX
Add		
Overhead Recovery Rate		XX
Add		
Profit Element		<u>XX</u>
Charge-out Rate		<u>XX</u>

* The element of Direct Labour Recovery Rate is effectively doubled in the calculation of Charge-out Rate.

Appendix II

Benchmark in Assisting Members to Extrapolate Audit Fees:

Recommended Basis Only

(A) Introduction

Audit fees shall generally be based upon the degree of responsibility, risk and skill involved and the time necessarily occupied on the work.

Empirical studies carried out by the Institute have shown a proportionate correlation between audit fees charged, based on time charge, and the value of total assets or gross turnover or operating expenditure. Therefore, for consistency and harmonisation of the fee levels, Council recommends that it is appropriate to determine audit fees using the Total Assets or Gross Turnover as shown in the financial statements and multiplying it with the coefficient percentages as shown in the coefficient percentage table (Appendix III).

The choice of Gross Turnover or Total Assets as the basis must be relevant and reflects closely to the time charge. Only where it is not appropriate to use Total Assets or Gross Turnover, members may adopt Total Operating Expenditure basis which must be relevant and reflect closely to time charge.

The guidelines for the determination of time charge is set out in Appendix I.

(B) Definitions

- (i) "Total Assets" is defined as the total of all assets as shown in the Balance Sheet.
- (ii) "Gross Turnover" shall mean and include:
 - (a) Total amount of sales including all other income and earnings for the year in the case of all manufacturing and trading organisations;
 - (b) Total gross premium income including all other income and earnings for the year in the case of all insurance organisations;
 - (c) Total amount of interest, discount, commission, exchange brokerage and all other income and earnings for the year in the case of banks and other financial institutions;
 - (d) Total amount of commission including all other income and earnings for the year in the case of travel agencies, indentors, brokers and other organisations whose principal source of income is commission earnings; and
 - (e) Total receipts/bills accounted for and all other income and earnings for the year in the case of construction companies and other entities not covered under (a) to (d) above.
- (iii) "Total Operating Expenditure" includes all expenses charged against gross profit to arrive at net profit before tax but excludes direct cost of sales.

(C) Computation Examples

Example 1

Assume that the Gross Turnover is RM1,740,000 and its Total Assets amount to RM2,560,000. The audit fees based on Total Assets and Gross Turnover will be computed as follows:-

On Total Assets:

First	100,000	at 0.8%	=	800
Next	150,000	at 0.35%	=	525
Next	250,000	at 0.25%	=	625
Next	500,000	at 0.15%	=	750
Next	1,500,000	at 0.10%	=	1,500
Next	60,000	at 0.08%	=	48
Total	RM2,560,000			RM4,248

On Gross Turnover :

First	100,000	at 0.8%	=	800
Next	150,000	at 0.35%	=	525
Next	250,000	at 0.25%	=	625
Next	500,000	at 0.15%	=	750
Next	740,000	at 0.10%	=	740
Total	RM1,740,000			RM3,440

However, the above determination must always be matched against time charge. Therefore, different jobs with different business activities and business structure may have the same Total Assets and Gross Turnover but the time incurred in performing the audit may vary.

For comparison purposes, if we use the above figures that has the same gross turnover and total assets but with different time charge for different companies audit, as follows:-

Company 1- RM3,400

Company 2 - RM3,600

Company 3 - RM4,000

Company 4 - RM4,500

the audit fees shall be determined as follows:

Company 1

Time Charge is relevant and closer to fees computed based on Gross Turnover. Thus, the recommended fee of RM3,440 will apply.

Company 2

Time Charge is between fees computed based on Total Assets and Gross Turnover. Thus the recommended fee will be based on time charge at RM3,600.

Company 3

Time Charge is relevant and closer to fees computed based on Total Assets. Therefore, the recommended fee will be RM4,248.

Company 4

Time Charge is higher than the fee calculated based on Total Assets. Therefore, the recommended fee will be on time charge at RM4,500.

Example 2

In a situation where an organisation has a Turnover of RM100 million and Total Assets of RM5,000 with total operating expenditure of RM1.5 million, it will be inappropriate to determine audit fees using the Total Assets or Gross Turnover basis because of the extremes.

Therefore, it will be appropriate to use Total Operating Expenditure.

Based on Total Operating Expenditure of RM1.5 million, the fee computed per the coefficient percentage table will be RM7,500 as follows :

The first	50,000	at 2%	=	1,000
The next	150,000	at 1%	=	1,500
The next	800,000	at 0.5%	=	4,000
The next	500,000	at 0.2%	=	1,000
Total	RM1,500,00			RM7,500

(D) Procedures for Implementing the Change in Audit Fees Billing

- (i) The revised recommended levels of audit fees shall be applicable **in respect of all statutory audits.**
- (ii) **The recommended levels of audit fees are applicable only for draft accounts submitted for audit with proper schedules.** Members may wish to charge higher audit fees having considered the reliance placed on internal control, complexity of business activity, volume of transactions, degree of responsibility and risk, skill of staff and timing of the audit etc.
- (iii) **Draft accounts submitted without proper schedules would require a member firm to utilise more skill and knowledge as well as time spent on the assignment, and as such the member firm should advise the client that higher audit fees may be charged for such audit assignments.**

Appendix III

Coefficient Percentage Table

(i) Gross Turnover or Total Assets Basis

Gross Assets or Turnover for every ringgit of		Rate(%)
RM		
The first	100,000	0.8
The next	150,000	0.35
The next	250,000	0.25
The next	500,000	0.15
The next	1,500,000	0.10
The next	2,500,000	0.08
The next	5,000,000	0.075
Above	10,000,000	Negotiable

(ii) Total Operating Expenditure Basis

Total Operating Expenditure for every ringgit of		Rate (%)
RM		
The first	50,000	2
The next	150,000	1
The next	800,000	0.5
The next	1,000,000	0.2
Above	2,000,000	0.1