

Please note this paper represents the PIE Issues paper (Agenda Item 6-A) for the September-October 2020 IESBA meeting and is provided to the Representatives for context only. Specific questions for Representatives are included in Agenda Item J (Cover Note) as well as Agenda Item J-1 (Presentation)

## **Definitions of Listed Entity and Public Interest Entity— Issues and Task Force Views**

### **OVERVIEW**

1. After reviewing comments received in Q2 and Q3, the Task Force has continued to develop its views and proposals with respect to:
  - The overarching objective for defining a class of entities for which the audits require additional independence requirements.
  - The approach to revising the definition of public interest entity (PIE), which consists of three key components:
    - (a) An expanded high-level list of broad PIE categories;
    - (b) An expectation that local bodies, such as regulators and oversight bodies, will refine the list as part of their adoption processes (through more explicit definition or establishment of size criteria); and
    - (c) A requirement for firms to determine if additional entities should be treated as PIEs.
2. In particular, the Task Force has made a number of revisions to the proposed text in **Agenda Item 6-B** for consideration by the Board at its September 2020 meeting. These include:
  - Refining the list of factors for assessing the level of public interest in an entity in proposed paragraph 400.8, including a potential new factor (Bullet #2).
  - Removing “additional” from “additional requirement and application material” in proposed paragraph 400.9 so that the proposals do not create the perception that audits of non-PIE entities are of lesser quality.
  - With regards to the list of high-level categories of PIE, revisions to subparagraphs (a) and (e) of proposed paragraph R400.14 (but no change to subparagraph (d) and no new proposed categories added).
  - Revisions to proposed paragraph 400.16 A1 to address the concern that some entities might be categorized by law or regulation as PIEs for purposes other than setting additional independence or audit quality-related requirements.
3. The Task Force also seeks the Board’s input on the following:
  - Whether, if the high-level PIE definition is simply adopted at local level without further refinement, firms should effectively be permitted to rebut the presumption that an entity falling within one of the broad categories is in fact a PIE.

- The draft options with regards to transparency disclosure developed by the International Auditing and Assurance Standards Board (IAASB) staff that will be presented to the IAASB for its consideration in November 2020.
- The Task Force’s approach to addressing the question of whether paragraph R400.20 should be revised so that the definition of audit client includes all related entities for all PIEs and not just listed entities.
- The effective date of the PIE final text, taking in account the effective dates for the Non-Assurance Services (NAS) and Fees final texts.

#### Matters for IESBA Consideration

IESBA members are asked to provide input to the following:

1. The Task Force’s analysis of Question #4 of the Exposure Draft, [Proposed Revisions to the Non-Assurance Services Provisions of the Code](#) (NAS ED).
2. The revised overarching objective as set out in proposed paragraph 400.9, and the supporting paragraph 400.8, in **Agenda Item 6-B**.
3. The Task Force’s revisions to the list of high-level categories of PIEs in paragraphs R400.14 to 400.16 A1 as well as the Task Force’s consideration of other types of entities.
4. The Task Force’s suggested approach of a limited rebuttable presumption as a means of reducing the risk of the high-level categories of PIEs being adopted at the local level without appropriate refinement.
5. The Task Force’s view and approach on addressing the issues of transparency disclosure and related entities.
6. The timing of the PIE exposure draft as well as the effective date of the PIE final revisions.

#### INFORMATION GATHERING ACTIVITIES SINCE JUNE 2020

4. In July 2020, the Task Force Chair and the IESBA Deputy Chair presented the key issues and the Task Force’s proposals to the IAASB. The IAASB was generally supportive of the Task Force’s proposed overarching objective and the broader approach to revising the definition of PIE. The key IAASB comments are discussed below in the relevant sections. See also **Agenda Item 6-D** for a copy of the draft minutes of that session. The next IAASB PIE session has been scheduled for November 10, 2020.



5. With the assistance of the IFAC Quality and Development Team (Q&D Team), the Task Force circulated a questionnaire (**see Agenda Item 6-E**) to approximately 40 professional accountancy organizations (PAOs) in Asia, Middle East and Africa as well as Central and South America in July and August 2020. The purpose of the questionnaire is to seek their input on the expected role and

capacity of local bodies to refine the PIE definition as part of the adoption process at the local level. The Task Force Chair will provide a verbal update at the September 2020 meeting.

6. In late August 2020, Task Force representatives also met with representatives from Accountancy Europe (AE) to seek their input. Amongst other matters, AE representatives acknowledged the Task Force's view that if there is already a PIE definition developed at the local level, there should not be much work to adopt the IESBA's revised definition by that jurisdiction. The Task Force Chair also agreed to review the proposed text to ensure that the expected role of local bodies and the enhanced role of firms are properly articulated.
7. IESBA staff has requested a meeting with the International Organization of Securities Commissions (IOSCO) and is awaiting its response. The Task Force is also working with the Q&D Team to gain a better understanding of any capacity issue faced by the francophone African nations, including possible assistance from the World Bank.

#### PIOB Public Interest Issues

8. In its July 2020 list of public interest issues on the IESBA work streams, the PIOB restated its previous view that it is crucial to determine the categories of entities (e.g. financial institutions, listed companies, significant utility companies), which should be subject to stricter provisions in the Code as the PIE definition affects other IESBA projects such as NAS and Fees. The PIOB noted that consideration should be given to any other entities that could pose a threat to financial stability. The PIOB also continued to highlight the importance of coordination between the IESBA and the IAASB to ensure consistent application of the two sets of standards.

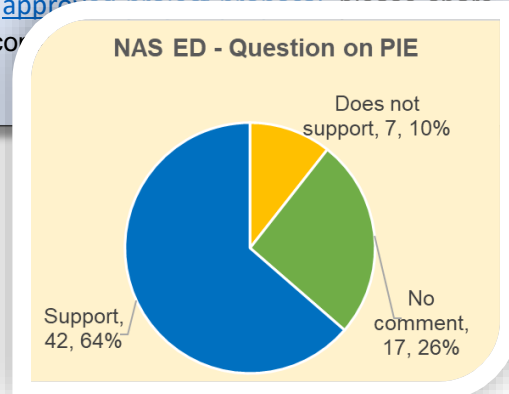
### **RESPONSES TO NON-ASSURANCE SERVICES EXPOSURE DRAFT<sup>1</sup>**

9. In January 2020, the IESBA released the NAS ED, in response to which the IESBA received 66 comment letters as of August 2020.
10. Question #4 in the NAS ED asked for respondents' views on the PIE project:

#### **NAS ED Question #4**

Having regard to the material in section I, D, "Project on Definitions of Listed Entity and PIE," and the planned scope and approach set out in the [approach paper](#), please provide your views about what you believe the IESBA should consider in developing the definition of a PIE.

11. Overall, the majority of respondents (90%) either provided feedback in support of the project or did not have any comments. Only 10% of the respondents did not support the project.
12. Having reviewed the main comments, the Task Force concluded that there were no new



<sup>1</sup> Refer to Appendix 2 of **Agenda Item 3-A** for a list of the respondents to the NAS ED and their abbreviations.

significant issues raised by the respondents to Question #4 of the NAS ED that either have not been addressed or are not being addressed by the Task Force and the Board.

### Key Comments from NAS ED Respondents and Task Force Responses

13. Some respondents acknowledged the importance of coordination with the IAASB to ensure appropriate alignment between the two Boards' definitions.<sup>2</sup> In this regard, from an early stage, the IAASB correspondent members have been actively participating in Task Force discussions and IAASB members have had the opportunity to provide their views at separate IAASB sessions. The two Boards have therefore been working to optimize the opportunities for convergence and alignment of definitions.
14. With regard to the overarching objective, the key comments raised were as follows:
  - There was express support from some respondents about different independence requirements for PIEs and non-PIEs;<sup>3</sup> only one respondent disagreed with such an approach.<sup>4</sup>
  - A few respondents highlighted the need to consider how financial statements are used by stakeholders, noting that for some entities, public interest might be focused on the services provided and, as such, historical financial statements may not be an important source of information for decision-making by stakeholders.<sup>5</sup>
  - The goal should be to promote uniformity across jurisdictions<sup>6</sup> but also allow for scalability at local level.<sup>7</sup>
  - A number of respondents provided input to the factors to be taken into consideration when determining whether an entity should be treated as a PIE.<sup>8</sup>
15. The Task Force noted that the key matters raised by the respondents with respect to the overarching objective have all been addressed by the Task Force. In particular, the Task Force reiterates its view that the focus of the overarching objective should be on building confidence in the audits of financial statements of PIEs, leading to additional independence requirements. The Task Force is also continuing to refine the list of factors in proposed paragraph 400.8 for the Board's deliberation.
16. With regard to the list of high-level PIE categories set out in proposed paragraph R400.14 in **Agenda Item 6-B**, the key comments raised were as follows:

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<sup>2</sup> **Firms:** GTI, PwC; **Independent NSS:** APESB; **PAOs:** BICA, CPAA, MIA, ICAS, WPK; **Public Sector Organization:** GAO

<sup>3</sup> **Regulator:** UKFRC; **PAOs:** AE, ISCA, MICPA

<sup>4</sup> **Public Sector Organization:** AGNZ

<sup>5</sup> **Firm:** KPMG; **PAO:** JICPA

<sup>6</sup> **PAOs:** HKICPA, MICPA

<sup>7</sup> **PAO:** JICPA

<sup>8</sup> **Firm:** NEXIA; **PAOs:** BICA, ICAEW, JICPA, NBAAT

- The Code’s definition should be simple, principles-based, and globally applicable to avoid unintended consequences.<sup>9</sup> It should take into account local definitions as well as allow for local refinements in order that the local definition can be set properly.<sup>10</sup>
  - Whilst some respondents expressed their support for a broader approach and have provided examples, such as large private entities and public sector entities, for the Board’s consideration,<sup>11</sup> other respondents preferred a baseline definition to which local bodies can add if necessary.<sup>12</sup> A few respondents also suggested consideration should be given to the IFRS definition of “public accountability entity.”<sup>13</sup>
  - There were queries about the term “listed entity” and the Board’s proposed revised definition of that term, such as whether entities with thinly traded equity or debt instruments should be captured.<sup>14</sup>
  - Some queried if the Code’s PIE definition will or should capture smaller entities<sup>15</sup> whilst others did not support separate treatment for smaller PIEs.<sup>16</sup>
17. The Task Force noted that the key matters raised by the respondents with respect to the proposed list of PIE categories have also been addressed by the Task Force. The Task Force also notes that:
- It had reached the conclusion that it would be difficult, if not impossible, to develop a single definition of PIE at a global level that can be consistently applied by all jurisdictions without significant modification and further refinement at a local level.
  - Its current approach is to develop a longer and more broadly defined list which local regulators or other authorities are expected to modify by tightening definitions, setting size criteria and adding or exempting particular types of entities. The Board generally supported this approach, subject to the outcome of the Task Force’s assessment of the capacity of local bodies to refine the PIE definition.
  - Many of the issues raised by respondents can be and should be best addressed at the local level.
18. A few respondents raised concerns about the capacity of local bodies to refine the definition in the Code.<sup>17</sup> As the Board is aware, the Task Force is currently seeking to address this issue and will brief the Board on the outcome of its information gathering with PAOs and its recommendations in due course.

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<sup>9</sup> **Regulator:** NASBA; **PAO:** AE; **Other:** SMPC

<sup>10</sup> **Firm:** BDO; GTI, Mazars; **PAOs:** ACCA & CAANZ, ASSIREVI, CAI, ICAEW, ICAS, SAICA, SAIPA, WPK; **Other:** EFAA

<sup>11</sup> **Regulator:** UKFRC; **Firm:** Mazars, **Independent NSS:** XRB; **Public Sector Organization:** AGSA

<sup>12</sup> **Firms:** EY, KPMG, PwC, **PAOs:** ISCA, MIA

<sup>13</sup> **Independent NSS:** APESB; **Others:** EFAA, SMPC

<sup>14</sup> **Firms:** Crowe, GTI, Mazars, PwC; **PAOs:** CPAC, WPK

<sup>15</sup> **Firm:** Mazars; **PAOs:** CPAC, CAI

<sup>16</sup> **Regulator:** IRBA; **Firm:** BKT

<sup>17</sup> **Firm:** PwC; **PAO:** CPAC

19. A few respondents raised the issue of related entities<sup>18</sup> which is also currently being addressed by the Task Force.
20. For those respondents that did not support the need to revise the definitions of listed entity and PIE, their reasons include:
  - The extant definitions are adequate.<sup>19</sup>
  - There might be unintended consequences of scoping in the wrong types of entities.<sup>20</sup>
  - The role of defining listed entities and PIEs belongs exclusively to local regulators.<sup>21</sup>
  - The project should be postponed due to a shift in public interest focus caused by the COVID-19 pandemic.<sup>22</sup>
21. Some respondents raised concerns about the timing of the NAS and Fees projects in light of the ongoing PIE project.<sup>23</sup> In particular, these respondents asked the IESBA to consider finalizing the NAS and Fees proposals only after the PIE project is completed in order that stakeholders can properly consider the impact of the NAS and Fees proposals. The Task Force understands that the Board will further discuss this issue at the September 2020 meeting in the context of the NAS and Fees projects.

## OVERARCHING OBJECTIVE

22. At its March 2020 meeting, the IESBA generally supported the Task Force's view that it is important at the outset to have clarity about the overarching objective for defining a class of entities for which the audits require additional independence requirements. This objective can then inform the approach and also provide a clear principle against which any proposals can be tested.
23. At its June 2020 meeting, the Board was generally supportive of the Task Force's revised draft overarching objective and the draft list of factors as set out in proposed paragraphs 400.8 and 400.9, with the majority of comments relating to the draft list of factors:
  - A few IESBA members queried if confidence in an entity meeting the necessary environmental, social and governance (ESG) criteria should be included in the overarching objective or as a factor for consideration. In response, Mr. Ashley reminded the Board that Part 4A of the Code deals with the independence of auditors of financial statements and that, before considering the independence requirements for ESG auditors, it would be important to articulate the role of ESG auditors more clearly.
  - Some IESBA members queried if the factor relating to potential systemic impact is more suited as an explanation of significant public interest. In response, Mr. Ashley noted that not all entities with significant public interest will have a systemic impact on the economy. Other IESBA

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<sup>18</sup> **Regulator:** IRBA; **Firm:** GTI

<sup>19</sup> **Regulator:** MAOB; **Firm:** ICAG,

<sup>20</sup> **Regulator:** NASBA

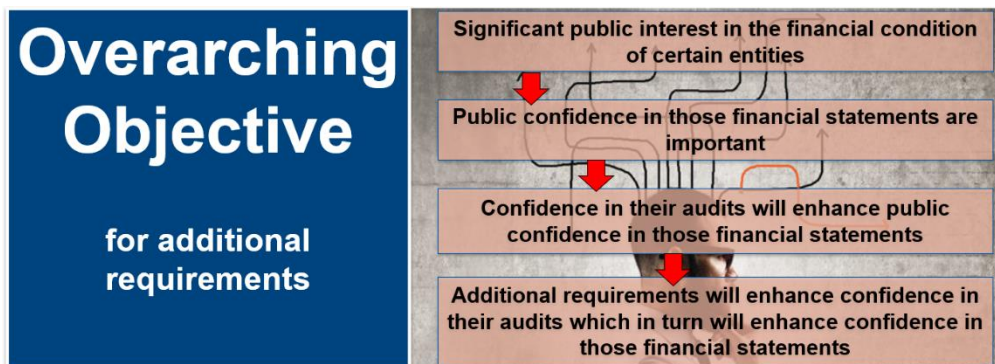
<sup>21</sup> **Firm:** RSM; **PAO:** CNCC

<sup>22</sup> **Firm:** Moore

<sup>23</sup> BDO, DTIL, EY, ACCA & CAANZ, CPAA, SMPC

members were comfortable with retaining the potential systemic impact of an entity as a factor for assessing the level of public interest.

- An IESBA member queried if any unlisted market operators as well as stock and commodity exchanges are sufficiently covered in the draft list of factors given their potential impact. The Task Force Chair undertook to consider further the role of such financial infrastructure parties, bearing in mind the importance or otherwise of their financial situation as opposed to their operational resilience. Another IESBA member suggested that consideration be given to whether those entities subject to regulation (specifically financial or prudential regulation) should be separately included.



24. At its July 2020 meeting, the IAASB was broadly supportive of the idea of an overarching objective for additional requirements to enhance confidence in the audit of certain entities and that the same overarching objective is applicable to both Board's standards. Amongst other matters, the following key comments were raised by IAASB members:

- As the proposals are developed, it would be important to avoid creating the perception that audits of non-PIE entities are of lesser quality.
- Whether the meaning of the term "financial condition" in proposed paragraph 400.8 is sufficiently clear.
- The difference in objectives between the two Boards and whether such difference might lead to minor differences in how the overarching objective should be expressed in the two Boards' standards.

### Task Force Responses

25. Following deliberation, the Task Force agreed to the following with respect to paragraphs 400.8 and 400.9 in **Agenda Item 6-B**:

- The term "financial condition" in the lead-in sentence in proposed paragraph 400.8 should be retained taking into account the need to put the role of the financial statements into context. In this regard, the Task Force shares the view of some IESBA members that whilst many may not necessarily review financial statements specifically, they will take confidence that the financial statements have been properly audited and that independence standards the relevant firms have complied with are at a higher level.
- The addition of a new factor (Bullet #2) concerning whether an entity is subject to financial or prudential regulatory supervision designed to give confidence that the entity will meet its

financial obligations. The Task Force would however specifically ask the Board to consider whether this criterion will capture anything not already caught by Bullet #1.

- Expanding Bullet #4 to include the concept of substitutability (although that word was itself felt to be problematic, particularly in translation) to capture a characteristic that is common to a number of public utility entities and financial market infrastructure entities (FMIs).
- Retaining Bullet #6 regarding the notion of systemic impact as one of the factors.
- No changes be made to the overarching objective with respect to ESG disclosures. It was noted that whilst ESG reporting (particularly for listed entities) is gathering pace across the globe, the role of ESG auditors is not always significant or globally consistent.
- Removal of “additional” in paragraph 400.9 in response to IAASB comments about a potential perception of two levels of audit quality.
- No change is currently needed to reflect any minor differences in how the overarching objective should be expressed in the two Boards’ standards. Should the IAASB feel that it should express the objective differently, the Task Force would expect a dialogue between the Boards at that stage that would lead to either alignment or a clear rationale for the distinction.

#### **Replacing Listed Entity with PIE in International Standards on Auditing (ISAs)**

26. The definition of the term “listed entity” in IAASB standards is identical to that in the Code. The term is used in IAASB Standards specifically in relation to requirements for:
- Communication of certain matters to those charged with governance (TCWG) in an audit of financial statements in ISA 260 (Revised), *Communication with Those Charged with Governance*.
  - Reporting for audits of financial statements of listed entities in ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*.
  - Communication of key audit matters in the auditor’s report in ISA 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*.
  - Reporting on other information for audits of financial statements of listed entities In ISA 720 (Revised), *The Auditor’s Responsibilities Relating to Other Information*.
  - The performance of an engagement quality control review for an audit of financial statements pursuant to International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*. The reference to “listed entity” is retained in the latest draft of proposed ISQM 1<sup>24</sup> ([proposed paragraph 34\(f\)\(i\)](#)).
27. The term “listed entity” is also included in the proposed ISQM 1 as an example of a factor for consideration under the material on scalability when a firm develops a system of quality management ([proposed paragraph 10](#)).

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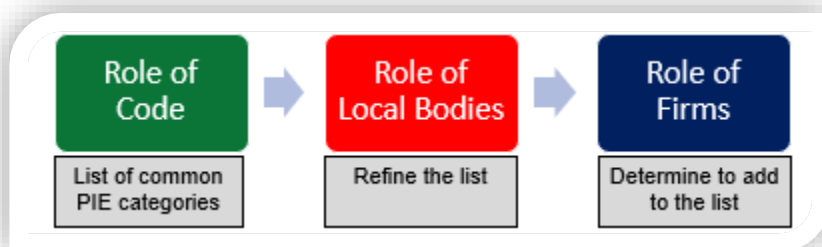
<sup>24</sup> Proposed International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*



28. At its July 2020 meeting, the IAASB agreed in principle with the Task Force's suggestion of replacing the term "listed entity" with "PIE" in the IAASB standards. However, a few IAASB members suggested that there would be merit in reviewing the use of "listed entity" in IAASB standards on a case by case basis to determine if such replacement would be warranted. In this regard, a few IAASB members also pointed out that there might be compelling reasons to retain the term "listed entity" without being inconsistent with the approach of a common overarching objective.
29. Given its current projects, it seems unlikely that the IAASB will have the necessary capacity to commence a review of the use of "listed entity" in its standards before early 2021. As such, the Task Force intends to include a question in the Exposure Draft to seek views on whether the term "listed entity" should be replaced by "PIE" in the IAASB's standards. This will allow the IAASB to analyze the information received at the start of its review of the use of "listed entity" in the ISAs.

## DEFINITION OF PIE

30. Both the IESBA and the IAASB have expressed general support for the Task Force approach:
- The development of a longer and broader list of high-level categories of entities as PIEs;
  - Refinement by national bodies by tightening definitions, setting size criteria and adding or exempting particular types of entities; and
  - Determination by firms if any additional entities should be treated as PIEs.



## List of PIE Categories

31. The Task Force proposed the following list of high-level PIE categories to the IESBA and IAASB in Q2:
- An entity whose shares, stock or debts are publicly traded
  - An entity one of whose main functions is to take deposits from the public
  - An entity one of whose main functions is to provide insurance to the public
  - An entity whose function is to provide post-employment benefits
  - An entity that pools money from the public to purchase shares, stock and debts
  - An entity specified as such by law or regulation
32. In reviewing the proposed list, both Boards have taken into account the Task Force's attempt to include only categories that will (possibly with tighter definitions and subject to size criteria) be accepted by most countries, and equally, to exclude entities that are only likely to be regarded as necessary by a minority. The Task Force's rationale also included the expectation that as part of the

adoption of the Code, local bodies will scope out those entities within these categories that are too small to be treated as PIEs and potentially scope in other entities as PIEs based simply on their size.

33. With regards to category (a) above:

- A few IESBA members suggested the use of the term “securities” and asked the Task Force to also consider the definition of “financial interest” in the Code:

*“An interest in an equity or other security, debenture, loan or other debt instrument of an entity, including rights and obligations to acquire such an interest and derivatives directly related to such interest.”*

- In response to queries raised by a few IESBA members about the phrase, the Task Force Chair clarified that the phrase “...being publicly traded” is used instead of “being listed” because some securities are only listed but not traded.

34. With regards to the Task Force’s query about whether to include in the description of category (a) those entities whose shares, stock or debts are in the process of being publicly traded, a few IESBA members:

- Expressed support for the Task Force’s alternative suggestion of including the concept as a factor for consideration by a firm.
- Suggested that it would be difficult to expand the concept to the other proposed PIE categories.

35. With regards to categories (b) to (f):

- There were some concerns that category (d) as drafted is too broad and may inadvertently capture employers that provide post-employment benefits such as those for executive teams.
- A few IAASB members queried if category (f) is necessary or appropriate on the basis that:
  - Local bodies will make the necessary adjustments anyway.
  - When a regulator determines what constitutes a PIE and the type of entities that should be included, that decision may not be driven by the same public interest considerations that are driving the IESBA’s focus on independence and the IAASB’s focus on audit standards.

#### Task Force Responses

36. Following deliberation, the Task Force has formed the following views and is suggesting the following changes to the proposed paragraphs R400.14 and R400.16:

- In category (a), replace “shares, stock or debts” with simply “equity or debt instruments” to better align with the definition of “financial interest” in the Code. The revised term is sufficiently broad to cover local variations.
- Regarding category (d), no change is proposed on the basis that:
  - The phrase “whose function” means employers that also provide post-employment benefits as just one of their activities would not be captured.
  - The current wording will capture both pension funds available to the public and those that are closed but nonetheless large enough to be considered as PIEs – subject to local determination on where to draw that line as for all the categories of PIE.

- Revise category (e) to more accurately describe investment funds, such as mutual funds, that are available to the public. The rationale for this revision is that:
    - If the financial instruments are not redeemable, they would invariably be caught by category (a) as that would be the only means for the public to “realize” their investment.
    - The revisions aim to restrict the definition to the “issuing” entity, i.e., the fund itself, and not to capture the fund management company.
  - Revise paragraph 400.16 A1 to address the concern raised by some IAASB members about an entity being categorized by law or regulation as a PIE not for the purpose of additional independence or audit quality-related requirements
37. With regards to the question of whether the term “listed entity” should be removed from the Code in light of the introduction of category (a) to the proposed expanded list of PIEs, the Task Force agreed to revisit this point when it reaches a view on whether to expand the categories of related entities relevant to listed entities in paragraph R400.20 to all PIEs (see discussion below).

### **Other Possible Categories**

38. At the June 2020 meeting, the IESBA discussed if custodians of assets or cash should be included as PIEs, taking into account the arguments for and against such inclusion. There was no strong support from the Board to add custodians as a new category, with a few IESBA members acknowledging the difficulty of developing a description for a global list.
39. The IESBA was also generally supportive of the Task Force’s conclusion not to include other categories of entities that it had considered, which include charities, public utility entities, public sector entities, large private companies, private equity funds, systemically significant entity and public accountability entity.
40. The Task Force Chair agreed that the Task Force will further consider financial market infrastructures (FMIs), stock and commodity exchanges as well as audit firms as possible categories of PIEs.

### FMIs, Stock and Commodity Exchanges

41. In the [Principles for Financial Market Infrastructures](#) (PFMI) of the Committee on Payment and Settlement Systems of the International Organization of Securities Commissions (IOSCO), FMI is defined as:
- A multilateral system among participating institutions, including the operator of the system, used for the purposes of clearing, settling, or recording payments, securities, derivatives, or other financial transactions*
42. FMIs play a significant role within the financial system and are considered to be systemically important. Safe and efficient FMIs are essential for a stable and well-functioning financial system. This means they require sound design and high standards of operational and financial resilience. FMIs can be structured in a variety of forms, including associations of financial institutions, nonbank clearing corporations, and specialized banking organizations. They may also be owned and operated by central banks or by the private sector and can be either for-profit or not-for-profit. FMIs may include payment systems, central securities depositories, securities settlement systems, central counterparties and trade repositories.

43. Similarly, stock and commodity exchanges play an important role within the financial system and the wider economy by providing the infrastructure, facilities and regulatory environment that allow businesses, industries and governments to raise capital, and investors to buy and sell various types of financial instruments. Many stock exchanges today are listed entities themselves and are therefore already classified as PIEs under the extant Code's definition.
44. The Task Force noted that some local jurisdictions, such as Singapore, Romania and South Africa, have included FMI and stock exchanges as PIEs in the local definition of PIE.
45. Following deliberation, the Task Force is of the view that the FMIs, stock and commodity exchanges should not be added as a global category of PIE for the following reasons:
  - Whilst the health of FMIs, stock and commodity exchanges is clearly important to the proper functioning of financial markets, given their typically large size, lack of substitutability in the markets they serve, and strong connections with banks and other financial institutions, the Task Force is of the view that the public interest in these entities relates more to their operations (including compliance with all necessary legal requirements) than their financial conditions.
  - The legal structure of such entities varies considerably between jurisdictions. For instance, as noted many stock exchanges are now listed entities in their own right and would therefore be treated as a PIE for that reason. Some, in contrast, are still mutual organizations owned by their members that effectively support it from a financial perspective. Payment organizations are similar. For example in the UK, the payments services provider Pay.UK is effectively sponsored by the Bank of England and the major banks – the fact therefore that it is currently showing negative reserves in its financial statements is of little or no consequence to the public who depend on its operations.

#### Audit Firms

46. At the June 2020 IESBA meeting, the PIOB observer asked the Task Force to consider if audit firms should be added as a category of PIE.
47. After deliberation, the Task Force has formed the view that audit firms should not be added as a new category of PIE for the following reasons:
  - Whilst the profession plays a significant role in society, the public interest in audit firms relates primarily to audit quality and their compliance with auditing and independence standards, and much less on their financial condition.
  - Whether an audit firm needs to file and publish financial statements, and what needs to be produced, varies considerably depending on the firm's structure, size and the jurisdictional requirements. Many audit firms are still established as partnerships and their financial condition is heavily linked to the position of individual partners.

### **EXPECTED ROLE OF LOCAL BODIES**

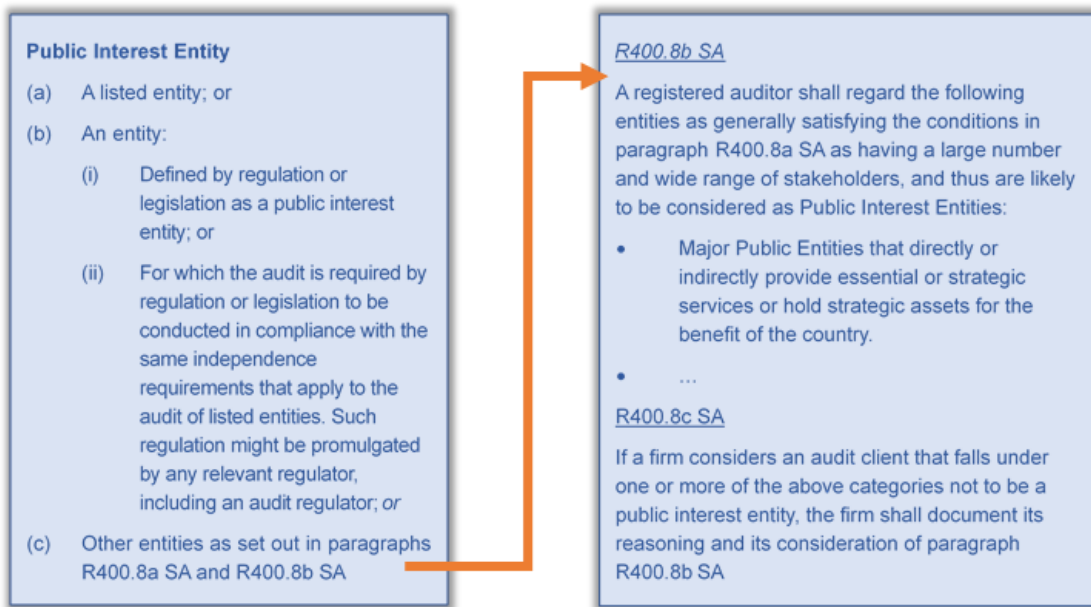
48. Given the high-level nature of the proposed expanded list of PIEs, the Task Force approach requires local bodies to assess and determine which entities or types of entities should be treated as PIEs for the purposes of additional independence requirements.
49. The Task Force is of the view that local bodies, be it the national standard setters (NSS), regulators, oversight authorities or other relevant bodies, are also best placed to consider the issues, concerns

and nuances specific to the local environment and how the financial conditions of certain entities or categories of entities might impact the public interest in their jurisdictions.

50. The Task Force also considered the concerns raised by IESBA and IAASB members as well as other stakeholders with regards to the local bodies' capacity. Their concern is that some regulators may not have the requisite capacity, in the sense of capability, knowledge and resources, or the authority to make the necessary assessment and refinements to a list of high-level PIE categories in their local Code. Further, the Task Force recognized that some jurisdictions might simply adopt the Code as is without much or any refinement, a step which is pivotal to the Task Force's current broader approach.
51. As mentioned earlier, the Task Force Chair will provide a verbal update at the September 2020 IESBA virtual meeting on the responses received from PAOs on the capacity of local bodies to refine the Code's definition of PIE.

### **Rebuttable Presumption**

52. To address the issue of local bodies adopting the PIE definition without the necessary local refinements, resulting in some entities inadvertently being captured as PIEs, the Task Force is considering the viability of some form of rebuttable presumption under limited circumstances in the proposed text.
53. In this regard, the Task Force noted that the Independent Regulatory Board for Auditors' (IRBA's) *Code of Professional Conduct for Registered Auditors* (South African Code) uses a rebuttable presumption with respect to its additional list of PIE categories. The South African Code includes an extra list of PIE categories, in addition to the Code's extant definition of PIE. It is with respect to this additional list of PIE categories that the rebuttable presumption applies.
54. Under paragraphs R400.8b SA and R400.8c SA of that Code, whilst a firm must treat a listed entity as a PIE, it may consider an entity that falls within one of its additional categories of PIEs not to be a PIE. In such instances, the firm is required to document its reasoning and its consideration of paragraph R400.8b SA (See diagram below).



55. The Task Force is considering therefore whether building in a rebuttable presumption under certain circumstances would be a viable solution to address the concerns about the lack of capacity of local bodies and the risk of the high level categories being adopted without the necessary local refinement.
56. In the first instance, the Task Force would like to seek the Board's views and directional input on whether it is supportive of the Task Force pursuing the above approach of a limited rebuttable presumption as a means to reduce the risk of the high level categories of PIEs being adopted at the local level without refinement.
57. If the Board is supportive of the Task Force pursuing this option further, the Task Force would also be interested in the Board's views on the following:
- (a) How the determination might be made that the local regulator did not intend the broad categories as defined by the Code to be adopted without amendment (i.e., the failure to implement local refinements was intentional).
  - (b) Whether the discretion to allow some form of rebuttable presumption should itself simply be left to the local regulators.
  - (c) Whether allowing the rebuttable presumption will discourage local regulators from making the necessary refinements.

## ROLE OF FIRMS

58. Both Boards were generally supportive of the Task Force's proposal to elevate the application material in extant paragraph 400.8 to a requirement for a firm to determine if any additional entities, or certain categories of entities, should be treated as PIEs as well as the additional list of factors for consideration by the firm.

## Transparency Disclosure

59. At the March and June 2020 IESBA meetings, the Task Force had pointed out that one effect of its proposals may be increased uncertainty as to whether an entity has been treated as a PIE, particularly if this determination has been made by a firm rather than as established by law or regulation.
60. To address this issue, the Board agreed that the Task Force should explore with the IAASB the option of adding a requirement in the ISAs for auditors' reports to disclose whether the particular entity was treated as a PIE.
61. At the July 2020 IAASB meeting, the responses from IAASB members were split to the question of whether the auditor's report should disclose if the client was treated as a PIE. Whilst some IAASB members felt that such disclosure would be unnecessary, others were supportive of the suggestion and were open to further explore this option.
62. Following discussions between IESBA and IAASB representatives, including the IAASB Technical Director and the IAASB Auditor Reporting Implementation Working Group Chair, IAASB representatives developed the following options for consideration by the IAASB at its next PIE session in November 2020:

#### Option 1

- No change be made to the auditor's report as the statement on independence as required in ISA 700.28(c) already refers to "the relevant ethical requirements relating to the audit," which implies as applied given the facts and circumstances of the entity.
- Whilst this option does not address the aim of enhancing transparency, it may appeal to those IAASB members who hold a view that a statement in the auditor's report that an entity was treated as a PIE will effectively introduce a 'two-tier audit'. In addition, there may also be a concern in terms of potential other unintended consequences and whether there might be any uncertainty about what constitutes a PIE for the purposes of the report.

#### Option 2

- The IAASB to pursue the possibility of enhanced transparency as part of its Auditor Reporting Post-Implementation Review, which is currently being undertaken.
- This option gives an opportunity for the IESBA to first settle on the proposed revisions to the definitions of PIE and Listed Entity, and for the IAASB and its stakeholders to consider more fully any changes and potential unintended consequences.
- This is unlikely to be an attractive option for the IESBA from a timing and convergence point of view.

#### Option 3

- The IAASB to consider draft revisions to ISA 700.28(c) in accordance with the proposed transparency requirement in the Code at the November 2020 IAASB PIE session.

## **RELATED ENTITY**

### **Background Information**

63. The concept of related entity is currently under review by four of IESBA’s ongoing projects: NAS, Fees, Engagement Team – Group Audits (ET-GA) and PIE. The key questions for each project are as follows:

Project	Key Questions
NAS & Fees	Which related entities of a PIE audit client should be scoped in under the revised provisions?
NAS	Does the self-review threat prohibition apply to parent undertakings that are unlisted entities?  Should a firm provide a NAS to an unlisted parent of a PIE audit client without information being provided to/concurrence obtained from TCWG of the PIE audit client?
ET-GA	What is the scope of related entities with respect to which component auditors outside the firm’s network should be independent?
PIE	Whether the universe of related entities for an audit client that is a listed entity in paragraph R400.20 should be the same for all PIE audit clients?

64. The Task Force needs to consider the question identified above in relation to PIE given the potential for dropping the term “listed entity” from the Code.

65. The extant Code contains only one reference of “listed entity” in the International Independence Standards (IIS) that is separate from its treatment as a PIE. This reference, in paragraph R400.20, specifies which related entities are to be included with the audit client for independence purposes, as follows:

- When an audit client is a listed entity, reference to audit client will always include its related entities (upstream, downstream and sister entities).
- When an audit client is not a listed entity, references to an audit client includes those related entities over which the client has direct or indirect control (downstream only).



- When the audit team knows, or has reason to believe, that a relationship or circumstance involving any other related entity of the client is relevant to the evaluation of the firm's independence from the client, the audit team shall include that related entity when identifying, evaluating and addressing threats to independence.

## IESBA Code 2018

### Definition of Related Entity

An entity that has any of the following relationships with the client:

- a) An entity that has direct or indirect control over the client if the client is material to such entity;
- b) An entity with a direct financial interest in the client if that entity has significant influence over the client and the interest in the client is material to such entity;
- c) An entity over which the client has direct or indirect control;
- d) An entity in which the client, or an entity related to the client under (c) above, has a direct financial interest that gives it significant influence over such entity and the interest is material to the client and its related entity in (c); and
- e) An entity which is under common control with the client (a "sister entity") if the sister entity and the client are both material to the entity that controls both the client and sister entity

66. When determining not to treat the universe of related entities for a listed entity audit client to be the same for all PIE audit clients as part of its Independence project in mid-2000, the IESBA had formed the view that such an expansion would be overly broad and unnecessary to maintain independence for some entities of significant public interest such as many government-controlled entities. The explanatory memorandum to the 2006 Independence ED stated that:

*"...in the case of an audit client that is a non-listed entity of significant public interest, in certain circumstances, depending on the nature and structure of the client's organization, it may not be necessary to apply the enhanced safeguards applicable to listed entities to all related entities of the client to maintain independence. The IESBA also recognized that in the case of certain entities of significant public interest, including many government-controlled entities which do not have a typical corporate structure, application of the enhanced safeguard to all related entities is overly broad and unnecessary to maintain independence..."*

### **Task Force's Consideration**

67. In the first instance, the Task Force had considered whether there is any philosophical reasons for not extending the full set of related entities applicable to listed entities to all PIEs in paragraph R400.20 given their level of public interest (i.e., a prima facie case that the definition of audit client for all PIEs, not just listed entities, should include all related entities).
68. Whilst noting the position reached by the IESBA in 2006 with respect to its Independence project, the Task Force also believes that there could equally be many non-listed PIEs to which the enhanced safeguards should logically be applied. The Task Force noted that the IESBA's rationale for not extending the full set of related entities beyond listed entities at that time seemed to more about the nature of the upstream entity (e.g., a government body) that controls the PIE rather than the nature of the PIE itself. However, to the extent that there are a number of listed entities that are controlled

by government bodies, those government bodies will already be impacted. Accordingly, the Task Force is of the view that there is a prima facie case to expand the definition of audit client for all PIEs.

69. The Task Force then considered if there are any reasons that may rebut this prima facie case and that the full set of related entities should not be extended to all PIEs or at least some types of PIEs. In this regard, the IESBA has raised two particular concerns:

(a) Logistical Challenge

- There may be practical difficulty in identifying, and obtaining the necessary data relating to, all related entities for some non-listed PIEs. The Task Force has heard that mapping out the entire organizational chart of a non-listed entity can be challenging in some jurisdictions.
- Further, clients may not be timely with updating their information on acquisitions or divestitures and, therefore, it may be difficult for auditors to obtain accurate information.

(b) Sovereign Wealth Funds (SWFs)

- The expansion to PIE from listed entity within the related entity provision in paragraph R400.20 may also significantly restrict the choice of auditors for some entities. For example, it was noted that there are jurisdictions where SWFs and government provident funds have interest in a multitude of portfolio entities. One example is Temasek Holdings in Singapore which is a major shareholder of Singapore Airlines and Singtel, both of which are listed entities. One concern relates to the services that could be provided by the auditor of one of the portfolio companies to other related companies of the SWF. Whilst this issue already exists under the current Code, its impact might increase if a non-listed PIE client includes all the categories of related entities.
- Also, as highlighted in the 2006 Independence ED, it may be argued that additional independence requirements on entities such as government-controlled entities may not be necessary to maintain independence. In this regard, Task Force noted the exception for the definition of “related party” set out in ISA 550:

*“However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another”*

70. The Task Force further notes that the provisions which would apply to an expanded definition of audit client would include most of those in Sections 400-540 including Compensation Policies, Gifts and Hospitality, Financial Interests, Loans and Guarantees, Business Relationships, Family and Personal Relationships, Recent Service with an Audit Client, Serving as a Director or Officer of an Audit Client, Employment with an Audit Client, Temporary Personnel Assignments and Long Association (as regards the activities in the cooling-off period). In some jurisdictions, such as the UK, a more piecemeal approach has been taken as to which provisions should apply to an expanded definition of audit client. Whilst this may be one option, the Task Force does not believe that it is practical or desirable to undertake that work within the current project.

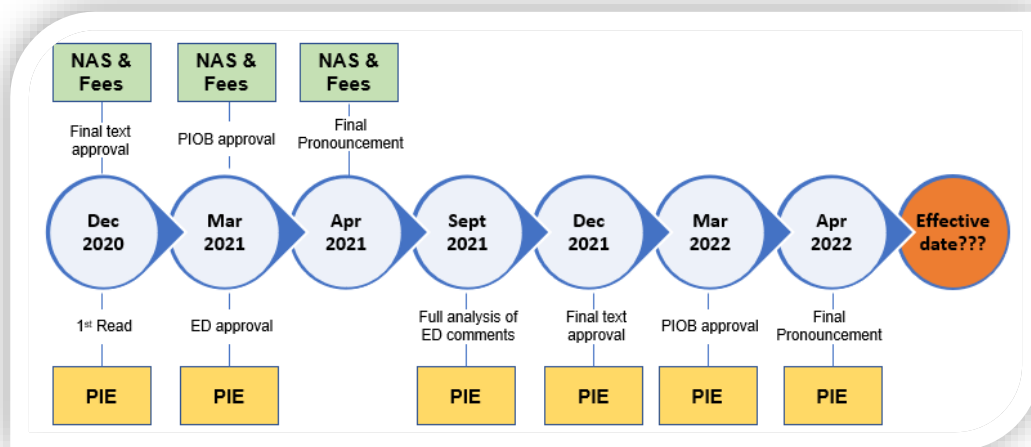
71. Other approaches that may be worth further consideration include:

- (a) Replacing “listed entity” in R400.20 by category (a) of proposed R400.14. This might be slightly complicated by the ability of local regulators to further refine these broad categories. Whilst it might expand the scope of audit client somewhat, it would clearly be less than for the expanded definition of PIEs.
  - (b) Allowing for local regulation to exclude specific types of related entity (e.g. government bodies) from the definition. This would permit recognition of specific local issues and structures but would obviously be less global in application.
72. The Task Force intends to seek input from the Forum of Firms (FoF) at its October 2020 meeting on the issue of related entity in light of a proposed expanded list of PIEs. The FoF participants will also be asked to give practical examples of how compliance with specific sections of the Code (e.g., Section 520) might be impacted by the suggested expansion to PIEs in paragraph R400.20.
73. The Task Force will provide its recommendations to the Board at the December 2020 meeting, but in the meantime would welcome any observations from the Board either on how best to approach the issue or on the issue itself.

## OTHER MATTERS

### Effective Date

74. The matter of the effective date of the final revisions to the PIE definition has become pressing given the impending finalization of the NAS and Fees projects.
75. One of factors in determining the actual effective date of the revised PIE definition will depend on the course taken on the project, i.e., whether the Board should approve a discussion paper in December 2020 instead of an exposure draft in either December 2020 or March 2021. In this regard, the Task Force has formed the view that given the progress of its proposals and outreach conducted to date, it is not necessary to develop a discussion paper prior to issuing an exposure draft.
76. Assuming it would be more efficient to issue the exposure draft in March 2021, potential milestones for the project would be as follows:



77. Key factors for consideration when determining the effective date for the revised PIE definition include the following:

- Under the Task Force’s current approach, time needed for local regulators and/or relevant bodies to refine the PIE definition and categories as part of their adoption process.
  - Whether to allow for a transition period for firms, including members of FoF networks, to operate on the basis of the extant definition pending promulgation of any necessary refinements to the list of PIE categories at the jurisdictional level.
  - How that approach should be aligned with the effective dates for the revised NAS and Fees projects, bearing in mind their anticipated issuance in April 2021.
78. There will be an opportunity for the Board to further discuss the effective dates of the NAS, Fees and PIE pronouncements at the September 2020 meeting.

**Next Steps**

79. The Task Force will present its proposals to:
- The IESBA CAG in October 2020
  - The IAASB in November 2020
80. The Task Force will seek written input from FoF participants on the issues relating to related entity.
81. The Board is asked to discuss the timing of the exposure draft in light of its discussion of the Task Force’s responses and proposals during the September 2020 meeting.