

Agenda Item N.2

Audits of Less Complex Entities—Issues

Objective of the Agenda Item:

This Agenda Item sets out further matters for Board consideration in relation to Audits of Less Complex Entities (LCEs). The objective of this Agenda Item is to obtain the Board's views on these matters to enable the LCE Working Group to develop its recommendations on the way forward¹ in relation to audits of LCEs for the IAASB's consideration at the June 2020 IAASB meeting.

I. Background and Introduction

Background

1. At the December 2019 IAASB meeting, the LCE Working Group presented [Agenda Item 6](#), which summarized the feedback from respondents to the Discussion Paper (DP), [Audits of Less Complex Entities \(LCEs\): Exploring Possible Options to Address the Challenges in Applying the ISAs](#), and related outreach². This agenda item also set out a broad direction for future IAASB actions, taking into account the views of respondents to the DP, to address the challenges that had been identified when auditing LCEs. The Board provided views to the LCE Working Group on the broad direction proposed for a way forward.
2. The responses to the DP strongly suggested that there is an urgent need to have an international solution to address issues related to audits of LCEs, in particular as jurisdictions develop standards and commence other initiatives in this area. In the view of the LCE Working Group, it would not be in the public interest for the IAASB to not focus on a response to the issues and challenges of auditing LCEs as a matter of priority.
3. Although the DP had focused on audits of LCEs, there was also a strong message in the responses to the DP that many of the issues within the ISAs related to more than audits of LCEs. Accordingly, two workstreams were identified:
 - (a) An 'ISA Focused Workstream' which would address the complexity, readability, understandability, scalability and proportionality issues in relation to the ISAs more broadly in order to address challenges that have been identified in applying the ISAs, for audits of all types of entities, including audits of LCEs; and
 - (b) A 'Separate Standard Workstream' exploring the possible development of a separate standard to focus on addressing the challenges in applying the ISAs in an audit of an LCE.
4. In considering the responses to the DP, there was an acknowledgement by the IAASB that a combination of actions would likely be needed to address the challenges and issues identified in the DP. However, before committing to specific further actions, the Board encouraged the LCE Working Group to further understand the issues raised by respondents so that appropriate actions could be

¹ Project proposals for specific Board actions will be developed for each workstream at the appropriate time.

² The International Federation of Accountants (IFAC) undertook a survey based on the DP to gather feedback from various stakeholders. 1,706 responses were received from 142 jurisdictions. Further information about the IFAC Survey is available in [Agenda Item 6](#), which summarized the feedback from respondents to the DP and related outreach.

recommended. Furthermore, the LCE Working Group was encouraged to explore the feasibility of the specific actions being considered in relation to an ISA focused workstream, and a workstream related to exploring the development of a separate standard for auditing LCEs. In the view of the LCE Working Group each workstream should inform the other. Draft minutes from the December 2019 IAASB discussions can be found in **Appendix 1**.

5. This paper presents the LCE Working Group's further considerations about how the work may be undertaken for each of the two possible workstreams, setting out some initial working group thinking about how this may be done. In addition, other matters that relate to both workstreams have been identified (see Section IV of this paper), which will also need to be addressed by the IAASB (i.e., not necessarily as part of any future projects from this specific initiative, but consideration will need to be given about how to best undertake this work). The Board's views on these matters will help the LCE Working Group in its development of more specific recommendations for future IAASB action to be presented for Board agreement at the June 2020 IAASB meeting.

Approach to the Board Meeting

6. The Chair of the LCE Working Group will briefly introduce the session, followed by Board discussion on each of the following areas:
 - Approach to Revising the ISAs (i.e., ISA Focused Workstream) (See **Section II** below).
 - Approach to exploring the development of a Separate Standard (i.e., Separate Standard Workstream) (See **Section III** below).
 - Other related matters (See **Section IV** below).

Appendices and Supplements Accompanying This Paper

7. **Appendix 1** to this Agenda Item provides an extract from the Draft minutes from the December 2019 IAASB LCE discussions.
8. **Appendix 2** to this Agenda Item provides an overview of the LCE Working Group and its outreach activities since December 2019.
9. **Supplements A to D** to this Agenda Item have been provided for reference purposes, and include:
 - **Supplement A**—provides an illustration of the exploratory work about the “building-blocks” in ISA 300, *Planning an Audit of Financial Statements*. This Supplement supports the discussion in paragraphs 23-34.
 - **Supplement B**—presents a staff illustration of how the ISAs could be revised, using the example of ISA 300, *Planning an Audit of Financial Statements*. This Supplement supports the discussion in paragraphs 49-50.
 - **Supplement C**—presents a high-level mapping of the content of the “LCE Specific Standard” (as referenced in paragraph 62(c)) to the ISAs;
 - **Supplement D**—provides detailed mapping of the objectives and requirements of the LCE Specific Standard (as referenced in paragraph 62(c)), as they relate to planning to the objectives and requirements of ISA 300, *Planning an Audit of Financial Statements*.

Introduction

High-Level Description of the Workstreams

10. The following sets out a high-level summary of what is explained in the relevant sections of this Agenda Item, and is intended to illustrate the breadth of the possible work. The two workstreams, and other related matters to be addressed, are broadly described as follows:

	<i>ISA Focused Workstream (Section II)</i>	<i>Separate Standard Workstream (Section III)</i>	<i>Other Related Matters (Section IV)</i>	<i>LCE Working Group Notes</i>
<i>Focus:</i>	Broader focus on addressing challenges in all ISAs, including in audits of LCEs	Exploring the development of a separate standard(s) for Audits of LCEs	Individual elements to be dealt with independently	
<i>Objective:</i>	To address challenges that have been identified in applying the ISAs in audits of all types of entities	To provide an audit solution that addresses the challenges in an audit of an LCE	To address specific challenges that have been identified in applying aspects of the ISAs, which are relevant to both workstreams	<ul style="list-style-type: none"> Some of the challenges and issues will overlap (or are the same) Notwithstanding the synergies between the workstreams, there may be different solutions in addressing the issues and challenges It is expected that the progression of each workstream will likely inform (or impact) the others
<i>Possible Actions:</i>	Described in Section II of this paper	Described in Section III of this Paper	Described in Section IV of this paper	
<i>Possible Timing to Finalization of Pronouncement(s) (see diagram below):</i>	Shorter term development of drafting conventions and guidelines (approximately 2 years); revising the ISAs 3-4+ years thereafter	3–4 years	Dependent on specific actions, but it is envisaged that these would be shorter-term	<ul style="list-style-type: none"> The workstreams will run parallel The focus of this project is audits of LCEs. The LCE Working Group have a strong view that addressing the specific issues of LCEs should be progressed as quickly as possible (also taking into account the expectations of

	<i>ISA Focused Workstream (Section II)</i>	<i>Separate Standard Workstream (Section III)</i>	<i>Other Related Matters (Section IV)</i>	<i>LCE Working Group Notes</i>
				<p>stakeholders representing LCEs, as well as the time the IAASB has been considering these matters)</p> <ul style="list-style-type: none"> • Development of drafting conventions and guidelines will inform the development of a separate standard

11. The possible timing set out above takes into account the IAASB's due process steps (where applicable) including:

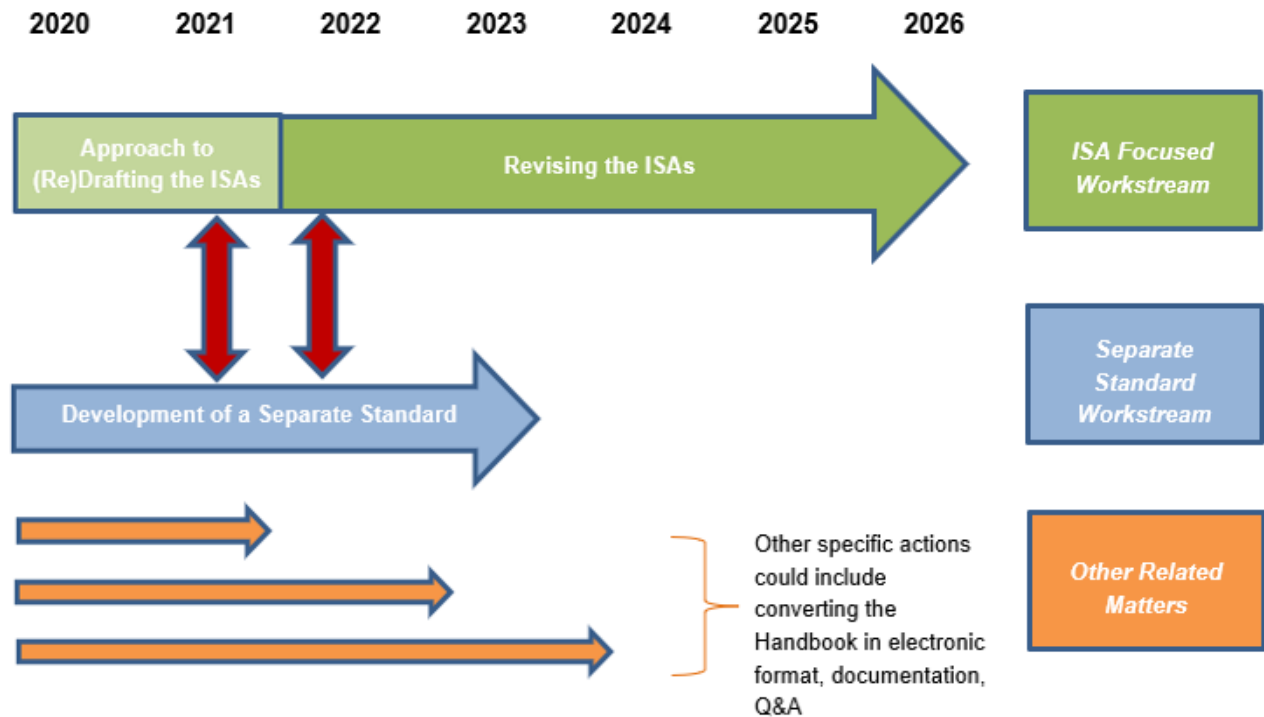
- The development, and approval, of a project proposal setting out specific actions to be undertaken.³
- The development, and approval, of a draft(s) of any new or revised pronouncement.
- Consultation on an exposure draft (ordinarily 120 days).⁴
- Making revisions to an exposure draft to address comments received on consultation. Also may require re-exposure depending on the nature and extent of revisions made.
- Finalization and approval of a final pronouncement(s), including setting the implementation date which may be 18-24 months after the final standard is published.

The ISA focused workstream, in particular, has various components, some of which may run concurrently and others which may run consecutively (for example the development of drafting conventions and guidelines for revising the ISAs, followed by the work to revise the ISAs).

12. The timing of the due process steps as described above may vary depending on the nature of the matters affecting the relevant pronouncement. In addition, in considering possible timing as set out above, the LCE Working Group has also been mindful of the focus in the IAASB's Strategy for 2020–2023 and Work Plan for 2020–2021 on being more agile in its standard-setting activities, while not compromising the required due process (i.e., balancing 'speed' and 'quality').
13. The graph below provides an illustration of the proposed activities by the LCE Working Group and the possible timing of each, including illustrating their synergies and the anticipated time from now to finalization (implementation of any pronouncement would likely be 18-24 months thereafter, but with early adoption allowed):

³ The project proposal for each Workstream would be developed, as appropriate, after the Board's approval of the recommendations at the June 2020 IAASB meeting.

⁴ This could be longer or shorter dependent on the pronouncement, with agreement by the IAASB.



II. ISA Focused Workstream

Highlights of Respondents Feedback Relevant to this Workstream

Challenges for IAASB related to applying the ISAs in Audits of LCEs:

- Overall length and volume of the standards
- Complexity was seen as an issue, as well as increasing level of prescriptiveness in standards
- Some prescribed procedures do not have a benefit or add little value
- Lack of support tools and guidance
- Specific ISAs highlighted include ISA 230⁵ (documentation), ISA 240⁶ (fraud), ISA 315 (Revised)⁷ (identifying and assessing risks) and ISA 540 (Revised)⁸ (accounting estimates)

Possible Actions Related to Revising the ISAs:

- Encouraged a 'building-blocks approach'
- Had mixed views about targeted approach versus a 'big bang'
- Would be most effective solution in addressing issues and challenges, but recognition that it may not be timely (i.e., there is a more immediate need for a specific LCE solution)
- Need simpler language and principles-based requirements
- Need more scalability and proportionality – for all entities, not only LCEs

⁵ ISA 230, *Audit Documentation*.

⁶ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*.

⁷ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

⁸ ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*.

14. This workstream would focus on what can be done to address concerns within the current suite of ISAs relating to:
 - Complexity.
 - Readability.
 - Understandability.
 - Scalability and proportionality.
 - Other issues noted by respondents to the DP that relate to the ISAs more broadly.
15. In discussing the possible actions that could be undertaken to address concerns about the ISAs more broadly, the LCE Working Group considered:
 - (a) The feasibility of a “building-blocks approach”, both in the context of the existing ISAs as well as rewriting the ISAs ‘from scratch’ using a “building-blocks approach”.
 - (b) If not a “building-blocks approach”, what else could be done to address the concerns that have been identified. In this regard, the LCE Working Group considered various matters relating to the way that the ISAs could be redrafted.

Exploring the Feasibility of a “Building-Blocks Approach”

16. There were respondents to the DP who encouraged the IAASB to consider comprehensively revising the ISAs using a “building-blocks approach”. In principle, the LCE Working Group is of the view that a “building-blocks approach” would encompass revising the standards by setting out the basic (i.e., fundamental or core) requirements for all audits, then expanding as needed to address more complex audit areas and specific circumstances.
17. The LCE Working Group undertook further exploratory work to consider the feasibility of the “building-blocks approach” in the context of the existing ISAs, to understand whether such an approach could be used effectively and what such an approach may entail. Work undertaken included:
 - A detailed review of respondents’ feedback to the DP, including consideration of possible suggestions about how a “building-blocks approach” to revising the ISAs could be used; and
 - For a selection of ISAs, a demonstration of how a “building-blocks approach” to revising the ISAs could be applied. This was done by analyzing and categorizing the requirements in the selected standards into core and other requirements (i.e., to identify and illustrate the “building-blocks”).

Review of Respondents’ Feedback to the DP

18. Respondents to the DP commented that by implementing an approach of “thinking small first” it should be possible to adopt a modular “building-blocks” format comprising a core set of general requirements applicable to every audit and then add additional requirements for more complex entities and those with a public accountability (i.e., a “core and more” basis). Respondents who advocated a “building-blocks approach,” also explained that such an approach could focus on the relevance and conditionality of each of the ISAs, as well as the individual requirements within each ISA. This approach is already described in the standards, as ISA 200⁹, paragraph 22, requires the

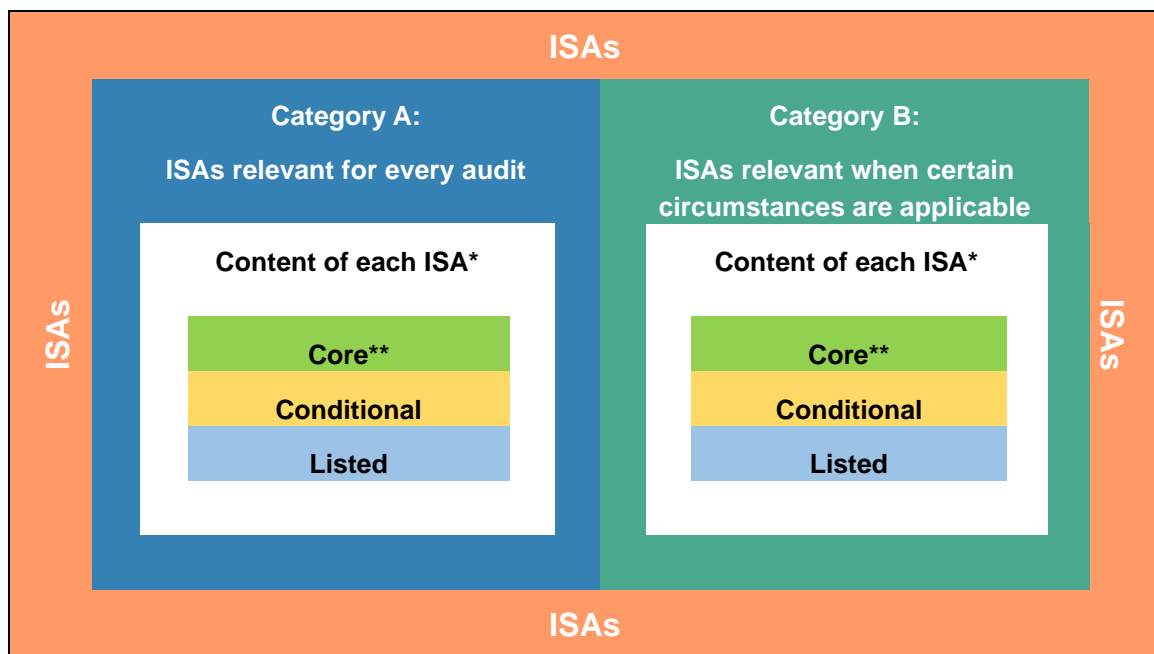
⁹ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

auditor to comply with each requirement of an ISA, unless, in the circumstances of the audit: (i) The entire ISA is not relevant; or (ii) The requirement is not relevant because it is conditional, and the condition does not exist.

19. Those respondents who encouraged using a “building-blocks approach” to comprehensively revise the ISAs indicated that it could be the ideal long-term solution, as the IAASB could retain one set of standards which would be appropriate for all stakeholders, regardless of size or complexity. Additionally, respondents expressed views that such an approach may result in greater compliance with the standards and would likely improve the quality of audits over the longer term.
20. Respondents also highlighted that this solution would allow audits of entities with one or more complex areas to continue to use one set of standards instead of having to move between different standards (i.e., full ISA vs a separate standard for LCEs), as well as avoid confusion when it comes to classifying and defining which entities should be designated as LCEs.
21. Respondents who encouraged this approach recognized that it would take substantial time and resources to complete such a revision across the entire suite of ISAs as it would require considerable work on each requirement within each ISA. There were mixed views by these stakeholders on how the revision should be undertaken (i.e., as one substantial project or on a rolling / incremental basis).

Demonstrating a “Building-Blocks Approach”

22. The diagram below illustrates how a “building-blocks approach” could be developed, taking into consideration the relevance and conditionality of the ISAs and their requirements, as discussed by respondents to the DP and taking into consideration the requirements of ISA 200, paragraph 22.



* The content of each ISA refers to all requirements within the Standards. Further consideration would need to be given to the application material.

** The core requirements would become the initial “building-blocks.”

Analyzing the ISAs

23. The initial exploratory work undertaken by the LCE Working Group Staff and reviewed by the LCE Working Group, included analyzing and identifying which ISAs are applicable to every audit, as well as analyzing and identifying the requirements that are conditional for a few selected ISAs.
24. As a **first step**, all extant ISAs related to an audit of financial statements¹⁰ were organized in two broad categories as follows:
- **Category A:** ISAs that are relevant for every audit; and
 - **Category B:** ISAs that become relevant only when certain circumstances apply.
25. The Standards included in Category A were those ISAs considered relevant for all audits, notwithstanding the size and complexity of the entity or the audit. This category consisted of most of the ISAs but there were challenges encountered (differences of opinion of the working group members) when classifying certain ISAs into one or the other distinct categories.
- Examples of Category A ISAs: the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance as covered in ISA 210, Agreeing the Terms of Audit Engagements, or the auditors' responsibility to plan an audit engagement, which are dealt with in ISA 300, Planning an Audit of Financial Statements.*
26. The Standards allocated to Category B included those ISAs that have 'conditional' application of that standard's requirements as a result of specific conditions triggered by the nature of:
- The Audit
Example: When the auditor expresses a modified opinion, the requirements of ISA 705 (Revised), Modifications to the Opinion in the Independent Auditor's Report, become applicable.
 - The Entity
Example: For listed entities ISA 701, Key Audit Matters in the Independent Auditor's Report, are relevant for communicating key audit matters in the auditor's report.
27. As a **second step**, a number of ISAs were selected covering the various stages of the audit process (i.e., from planning to reporting) and from each category of relevance as determined in paragraph 24 above (i.e., from Category A or B), for further analysis. The selected ISAs were:
- **Category A:** ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*;
 - **Category A:** ISA 300, *Planning an Audit of Financial Statements*;
 - **Category A:** ISA 500, *Audit Evidence*; and
 - **Category B:** ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*.

¹⁰ Further consideration will need to be given to the standards of the 800-899 ISA series, which become applicable for circumstances when the auditor performs an engagement in a specialized area, once a plan has been developed for actions in relation to the ISAs used for an audit of historical financial information.

28. The requirements within the selected ISAs were analyzed to identify and illustrate the “building-blocks” within each standard – i.e., each paragraph was categorized into the following:

Core	Applicable to every audit
Conditional	Applicable when specific circumstances are present
Listed	Applicable for listed entities

29. The “*core building blocks*” paragraphs were deemed to be requirements applicable to all audits (i.e., without considering complexity, size or any specific circumstances which may be present with the audit or the entity).
30. The “*conditional building blocks*” were deemed to be requirements that become applicable depending on facts and conditions linked to the audit (for example, the requirement to communicate with the predecessor auditor is only relevant for an initial audit engagement and when the previous period financial statements were audited by another auditor).¹¹
31. The “*listed building-blocks*” are requirements that are only applicable to listed entities (for example, the responsibility of the engagement partner to determine that an engagement quality control reviewer has been appointed for an audit of a listed entity).¹²
32. **Supplement A** sets out an extract from the work performed for ISA 300, *Planning an Audit of Financial Statements*, which has been presented to illustrate the work undertaken for one of the standards.

Working Group Observations

33. The LCE Working Group’s key observations from the work undertaken to explore the feasibility of a “building-blocks approach” are summarized below:
- (a) Categorizing the ISAs into broad categories based on their relevance (i.e., ISAs relevant for every audit vs ISAs relevant when certain circumstances are present), as well as mapping individual content of the standards to “building-blocks” (i.e., core, conditional and listed), helps to demonstrate the current applicability of the ISAs and provides evidence that the “building-blocks” principles are already largely embedded within the extant ISAs.
 - (b) In the context of the current structure of the ISAs, revising the ISAs using a comprehensive “building-blocks approach” (as contemplated above), would require a radical restructuring and rewriting the ISAs to achieve the objectives of revising the ISAs (in particular to address issues of scalability and proportionality). Such an approach would require substantial effort and Board capacity, which would likely significantly affect many ongoing and planned projects in the medium-term. Furthermore, such a comprehensive rewrite of the ISAs may also risk a proliferation of jurisdictions undertaking their own remedies with regard to the challenges being experienced when auditing LCEs. Moreover, the LCE Working Group is of the view that there could be other remedies for the issues and challenges that would not require such a fundamental rewrite of the ISAs.

¹¹ ISA 300, *Planning an Audit of Financial Statements*, paragraph 13(b).

¹² ISA 220, *Quality Control for an Audit of Financial Statements*, paragraph 19(a).

- (c) Notwithstanding a “building-blocks approach” may not be feasible, the “building-blocks” principles already exist in the ISAs, and the exercise undertaken has been helpful to the LCE Working Group in considering possible future actions to address the issues and challenges that have been identified:
- Relating to the concerns raised by respondents to the DP about the perceived overall length and volume of the ISAs when applied together, further reflection may be needed about how the ISAs are presented to better demonstrate the applicability of all of the ISAs / core requirements, which may add clarity about the scalability of the extant ISAs.
 - The analysis undertaken is a good starting point for further work by the LCE Working Group as it highlights the “core” elements of the ISAs, as well as the conditional application of the requirements within the Standards. However, although insightful and educational, in the view of the LCE Working Group, developing a “building-blocks approach” in such a way will likely not address the concerns that have been raised about scalability and proportionality.
34. Accordingly, the LCE Working Group has the view to not further pursue a “building-blocks approach” to comprehensively revise the ISAs. However, it was agreed that the learnings from exploring such an approach would be used to inform any revisions of the ISAs as well as the work undertaken in exploring the development of a separate standard for Audits of LCEs (i.e. aspects of the notion of “building-blocks” as described in this section may still be helpful in relation to both workstreams).

Developing an Approach to (Re)Drafting the ISAs

35. The next approach to comprehensively revising the ISAs considered by the LCE Working Group involved consideration of various matters relating to the way that the ISAs have been drafted (and in particular, the redrafting from some of the more recently completed projects). These considerations included:
- The drafting conventions developed during the IAASB's Clarity project.
 - The impact of new and revised presentation and drafting in the ISA 315 (Revised 2019) and ISA 540 (Revised) projects.
 - Scalability and proportionality of the ISAs.

Drafting Conventions and Guidelines for a Revised Presentation of the Standards

36. Respondents to the DP commented that should revisions to the ISAs be made, it would be beneficial to develop a new drafting framework for structural changes to the ISAs, including using clear, plain language, providing clarity about the documentation requirements, and avoiding duplication and repetition of requirements. Such a new drafting framework would help with greater consistency in understanding how the standards have been drafted, and in how the standards are to be applied.
37. In 2003, the IAASB undertook a review of the drafting conventions used in its standards as part of the IAASB's Clarity project. The objective of the review was to identify ways to improve the clarity, and thereby the consistent application, of the International Auditing Standards issued by the IAASB.
38. As part of the Clarity project, the “clarity drafting conventions” were developed for the purpose of Task Forces giving due regard to the constructs and terms used across the IAASB's literature when developing a new pronouncement, or revising an existing pronouncement. It was also intended to aid

readers by using the same or similar terms to mean to the same or similar actions or circumstances, to avoid complicating the ISAs.

39. The clarity drafting conventions were developed, to be adapted as necessary to differing circumstances, and set out the content of the scope, other introductory and objective paragraphs, including an explanation about how these should be drafted. The drafting conventions also provided context for the content of the requirements and application and other explanatory material, as well as an explanation of the drafting styles for these paragraphs. The drafting conventions also require the IAASB's pronouncements to follow the Chicago Manual of Style / AP Style Manual for matters of grammar and punctuation.
40. In addition, and more recently, in September 2019, the IAASB completed its project to revise ISA 315 (Revised 2019). On exposure, the IAASB received feedback about the complexity and understandability of the standard, (and standards in general), as well as the scalability and proportionality for all entities, but in particular those entities that are considered to be less complex (similar feedback was also received on exposure for ISA 540 (Revised), and also the quality management standards series).¹³
41. In response to the feedback on exposure, the ISA 315 Task Force developed principles for an enhanced presentation of the revised standard (the changes did not impact the drafting conventions developed during the IAASB's Clarity project which were explained above).
42. Specifically, the ISA 315 Task Force:
 - (a) Used simpler sentences and more straightforward language for each requirement.
 - (b) Combined or separated requirements, as appropriate, to enhance their understandability.
 - (c) Presented the requirements at a higher level and focused them on "what" has to be done, with additional explanation in the application material as to "why" the procedures are required (including related criteria which was seen as assisting with the implementation of the requirement).
 - (d) Addressed "how" a requirement may be executed elsewhere in the standard than in the requirements (for example, considering what further can be included in application material and appendices).
 - (e) Where appropriate, drafted requirements consistently (for example for each of the components of the system of internal control) so that it does not appear that one requires a different approach from another when that is not intended.
 - (f) Reduced cross-referencing within the requirements to reduce complexity.
 - (g) Addressed perceived inconsistencies in terms to avoid inconsistency in their application.
43. With regard to the application material, in addition to similar actions as described above, the ISA 315 Task Force also:
 - (a) Enhanced the supporting application material, as relevant, to explain "why" a particular requirement exists.

¹³ The quality management standards series includes three exposure drafts, 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*; ISQM 2, *Engagement Quality Reviews*, and International Standard on Auditing (ISA) 220 (Revised), *Quality Management for an Audit of Financial Statements*.

- (b) Placed examples within boxes to separately identify them and enhanced the examples as appropriate.
- (c) Moved guidance relating to the entity (rather than the auditor's considerations of the entity) to the Appendices.
- (d) Removed guidance better suited to implementation guidance.
- (e) Removed language that repeated the requirement.
- (f) Reconsidered, and revised where possible, long and complicated sentences and paragraphs.
- (g) Inserted section headings within the application material in a consistent way so that users of the standard are able to more easily navigate the standard.

Working Group Observations

44. The LCE Working Group has the view that as part of any project to revise the ISAs, the following would need to be further considered:

- As a first step, have a clearly defined set of drafting principles, which promote, among other things, clarity and consistency. An appropriate first set of drafting principles are the clarity drafting conventions, which underpin the drafting of the ISAs. In considering the clarity drafting conventions, determine whether any further changes are needed. As part of this work, the LCE Working Group has the view that the extant drafting conventions should be fully documented and made transparent so that there is a common understanding of how the standards are currently drafted. Inconsistencies would need to be identified and consideration given to how these should be addressed. It would also need to be explored whether there is anything else that needs to be done in relation to the clarity drafting conventions.
- Whether, and how, the presentation, drafting principles and rigor applied when revising ISA 315 (Revised 2019) could be applied to the other ISAs, including whether such changes would effectively address some of the issues and challenges identified, whether the changes would be appropriate for all standards and whether there could be other changes that could also be helpful.

A plan would need to be developed about how to develop and work through the changes that would be most effective and useful in addressing the challenges and issues identified.

Scalability and Proportionality of the ISAs

- 45. Some respondents to the DP expressed views that further clarity on the differences, interrelationships and connections between the concepts of scalability versus proportionality would be beneficial, as well as further building on the drafting principles developed as part of IAASB's Clarity project, with an additional focus on understandability of the standards.
- 46. Scalability and proportionality of the ISAs is essential to the use of the ISAs by entities of all sizes and complexities. As noted above, this is an area that stakeholders continually voice concerns about. In the IAASB's recently completed projects (ISA 540 (Revised) and ISA 315 (Revised 2019)), and those currently underway (in particular in relation to the quality management standards), this is a topic of ongoing consideration by Task Forces and the IAASB about what more can be done.
- 47. In the view of the LCE Working Group, as part of any project to revise the ISAs, further consideration will be needed as to how scalability and proportionality of the IAASB's standards can be further enhanced. As explained above, a "building-blocks approach" was one way of addressing some of the

related issues and concerns, however as noted, applying a comprehensive “building-blocks approach” would not adequately address the concerns that had been raised because the ISAs already contain elements of conditionality and there are a lot of standards/requirements that are core to all audits.

48. As part of the considerations about possible actions to be undertaken in the ISA Focused Workstream (i.e., revising the ISAs), the LCE Working Group notes that further work in this area will be informed by work done in current projects to enhance scalability and proportionality (for example through use of examples to illustrate how a requirement can be applied in circumstances that are both less complex and more complex).

Demonstrating the Revisions to the ISAs

49. Building on these drafting principles and considerations, the LCE Working Group staff undertook an exercise to demonstrate how possible revisions to a selected ISA could look like in practice. Similar to the “building-blocks” illustration in **Supplement A**, the LCE Working Group staff applied some initial thinking about how standards could be redrafted (using the same example of ISA 300, *Planning an Audit of Financial Statements*), which is presented in **Supplement B**. In doing so, the LCE Working Group staff considered and identified possible issues related to:

- Redundancy and repetitiveness of the requirements;
- Conditionality of the requirements;
- Using straightforward language (i.e., avoiding complexity in language and sentence structure) in the requirements so the auditor is clear what needs to be done;
- The need to use cross-referencing to other standards (to avoid repetition); and
- Consistency of terminology used.

This exercise is for illustrative purposes, and further consideration of further changes may be needed once appropriate drafting conventions and guidelines are agreed.

50. The work undertaken and presented in **Supplement B** is a staff exercise and is presented for illustration purposes only, as a more definitive revision could only be performed after developing and articulating the approach to (re)drafting the ISAs.

Timing for Revising the Suite of ISAs

51. Respondents to the DP expressed mixed views on the way the ISAs should be revised (i.e., all in one big project or on a rolling basis).
52. It was recognized that an approach of revising all the ISAs in one substantial project, similar to the Clarity project, would take a long time to complete and would use a lot of IAASB capacity (i.e., limiting what else can be undertaken by the IAASB at that time). On the other hand, respondents commented that targeted prospective revisions and/or retrospective changes on a rolling/phased basis by selecting the standards that would bring the most benefits for audits of LCEs, may come at the expense of involving years of incremental change.

Working Group Observations

53. The LCE Working Group recognizes that any project to revise the complete suite of ISAs would likely take a longer time to complete, and such work could commence only after the approach to (re)drafting the ISAs is developed, articulated and agreed.
54. In undertaking such a comprehensive project, the LCE Working Group has recognized the concern that opening up all of the standards could result in a substantial 'Clarity-type' project (i.e., some standards may need to be more fundamentally revised). It is the view of the LCE Working Group that the project would need to be carefully scoped and discipline maintained to ensure that the focus is on drafting and not changing the substance of the underlying requirements within the standards.
55. With respect to the expected timing of the revisions, the LCE Working Group is of the view that this decision can be made once the appropriate approach of the revisions has been determined.
56. The total estimated timing for revising the ISAs is based on an initial estimation of the work that may be undertaken in this workstream (i.e. approximately 2 years for developing drafting conventions and guidelines, with a further 3-4+ years to revise the ISAs depending on how this is done). Specific Board actions within this workstream are still subject to Board discussion and the actual work undertaken may vary from this initial assessment of what may be included, in which case the timing will likely vary. It is estimated that the development of the drafting conventions and presentation structure (including the due process involved and consultation thereon) could take approximately 2 years, based on the need to consider the most appropriate changes to be applied to the ISAs, and consultation thereon. The subsequent revision of the ISAs (including all the due process steps) could take 3-4+ years taking into account the IAASB's due process for such revisions (see paragraph 11). this also depends on maintaining discipline to ensure focus is on drafting and not re-evaluating the underlying requirements.

In Summary – Revising the ISAs Workstream

Based on the feedback from the DP, the LCE Working Group's deliberations and the work performed, the LCE Working Group would like to develop its recommendation to develop a plan for the ISA Focused Workstream which would involve:

- The initial development of 'drafting conventions and guidelines for presenting ISAs' (i.e., principles for drafting) to be agreed by the IAASB and its stakeholders. These conventions and guidelines would be developed to address the issues of complexity, readability, understandability and scalability and proportionality, and would be articulated so that there is a consistent use and understanding in the way that the standards have been written.¹⁴
- A decision as to how to revise the ISAs to apply the conventions and guidelines, (i.e., whether it would be as part of one significant project, or on some kind of rolling basis) once the drafting conventions and guidelines have been agreed.
- A project to revise the ISAs accordingly.

¹⁴ It is envisioned by the LCE Working Group that the development of these drafting conventions and guidelines would run parallel to the initial efforts in the development of a separate standard as explained in Section III, and any drafting of such a standard would also encompass any agreed changes to the style and articulation developed in this aspect of the ISA Focused Workstream.

Matters for IAASB Consideration

1. The Board is asked:
 - (a) Whether it agrees with the LCE Working Group's analysis to focus on revising the ISAs through developing agreed drafting conventions and guidelines in a separate workstream?
 - (b) For its views about the approach to revising the ISAs as has been set out in the summary above, including:
 - (i) Initially developing and articulating drafting conventions to be used for new and revised ISAs; and
 - (ii) Determining the most effective way to revise the ISAs to address the concerns and issues that have been identified?
 - (c) Whether there are any other matters the LCE Working group should consider as it develops its recommendations for a workstream to revise the ISAs?

III. Separate Standard Workstream

Highlights of Respondents Feedback Relevant to this Workstream

Possible Actions Related to Developing a Separate Auditing Standard for Audits of LCEs:

- More timely solution - would be quicker than revising all of the ISAs
- Needs to result in a reasonable level of assurance
- Little support for development of a separate standard using a different framework – any such standard must be based on the ISAs

Definition of the LCEs:

- Support for a principles-based approach using qualitative characteristics
- Further consideration is needed about what the qualitative characteristics are, including a number of suggestions about other risk-based factors
- Mixed views expressed on excluding 'listed' or 'public interest entities'
- Caution that any description of LCEs needs to be in the context of the outcomes of the IAASB's work – so that the description is relevant to those outcomes (for example if it is determined that a separate standard be developed, the description needs to be relevant to when that standard can be used). Therefore, a detailed discussion on the descriptive factors can wait until after the discussion of options for the way forward.

57. One of the options within the DP for addressing the challenges and issues related to audits of LCEs was the development of a separate standard for audits of LCEs. Based on the considerable feedback in the responses to the DP on the development of a separate standard (see paragraphs 52-53 and paragraphs 55-60 of [Agenda Item 6](#) from the December 2019 IAASB meeting), the LCE Working Group had discussed exploring a separate workstream to further consider whether there are benefits in addressing issues related to audits of LCEs through the development of a separate standard. In December 2019, the Board

broadly supported further consideration about this ‘Separate Standard Workstream’ (subject to the further work that the LCE Working Group was encouraged to undertake.

58. Notwithstanding respondents to the DP, encouraged the development of a separate standard using the ISAs as a base, the LCE Working Group explored three possible approaches:
- (a) Start afresh and completely draft a new standard, still using a risk-based approach to achieve reasonable assurance, but not using the structure or flow of the ISAs as a basis for the development of a new standard. However, such a standard could be drafted using agreed drafting conventions and guidelines (for example as developed in the ‘revising the ISAs’ approach explained in Section II above). Such an approach would likely take longer to develop as content and principles used would be different to the ISAs, and may be harder to demonstrate that reasonable assurance will be achieved.
 - (b) Use the existing ISAs as the underlying basis for a new standard, and making targeted, consistent changes (utilizing agreed rules such as removing conditionality, removing repetitions and cross references, etc.). Such an approach would be similar to the explanation of the “building-blocks approach” (with additional changes), although reducing the content of the ISAs, may not quite meet the expectations of stakeholders who are looking for a ‘simpler’ solution.
 - (c) A ‘hybrid’ version (i.e., a hybrid between (a) and (b))—using the same approach as (b) as a starting point, but redrafting where necessary to simplify or present the requirements in a revised presentation style. This approach would have the advantage that the basic structure of a risk-based audit that manifests in a reasonable assurance opinion would still be apparent, while making changes for brevity and focus on what is relevant in an audit of an LCE.
59. In its deliberations about these three options, the LCE Working group were of the view that option (a) could potentially drift away too far from the extant ISAs which would make (or appear to make) achieving reasonable assurance more difficult, and away from the calls from the respondents to the DP, while option (b) may partly address some of the issues and concerns identified but the final product may not address the full spectrum of issues and concerns.
60. Accordingly, in the view of the LCE Working Group, in exploring the development of a separate standard the ‘hybrid’ approach would be most appropriate. In its deliberations, the LCE Working Group recognized the overarching objective that a separate standard should enable the auditor to obtain reasonable assurance. In addition, consistent with the responses to the DP and the IFAC Survey:
- (a) The separate standard should be developed using a principles, risk-based, approach (which would be consistent with extant ISAs); and
 - (b) The separate standard should retain, and be seen to retain, the same credibility as the ISAs.
61. In considering the various options and what may be most effective and timely, the LCE Working group also took into account the following:
- (a) Basing the separate standard on the existing ISAs in some way would make it easier to develop a separate standard that would result in a reasonable assurance opinion (*to note*: the LCE Working Group would still need to consider the form of the opinion, that is how the opinion is expressed within the auditor’s report (for example, “in accordance with the ISAs” or “in accordance with the separate standard for LCEs”), but agree that this will need to be deliberated at a later point once

there is more clarity about the approach to developing a separate standard). A reconciliation back to the ISAs (presented as part of the consultation) would enable stakeholders to assess that the work performed using the separate standard would provide reasonable assurance (i.e., the content of the separate standard would be more familiar and it would be easier to bring the IAASB's stakeholders on the journey in a new space for the IAASB). Not being based on the existing ISAs would make it more difficult to assess that reasonable assurance has been obtained, but not impossible, as the IAASB has achieved this through other standards that also achieve reasonable assurance (i.e., ISAE 3000 (Revised)).¹⁵

- (b) The increasing proliferation of 'solutions' being developed by others to address the issues and challenges of auditing LCEs, and the more urgent need for a timely global solution.
62. In developing possible actions for exploring a Separate Standard Workstream, the LCE Working Group undertook an analysis of:
- (a) The initiatives of the various jurisdictions or regions that have developed a separate standard for audits of less complex (or smaller) entities (see paragraphs 63-65 below);
 - (b) The initiatives undertaken by other standard setting boards, such as the experiences of the International Accounting Standards Board® (IASB®) in developing the International Financial Reporting Standard for Small and Medium-Sized Entities (IFRS for SME® Standard) (see paragraphs 66-72 below); and
 - (c) The previous work undertaken, in early 2018, by an informal working group of the IAASB that prepared an example of what a standard for Audits of LCEs could consist of (referred to as the "LCE Specific Standard") (see paragraphs 73-75 below).

Considering Jurisdictional and Regional Initiatives Targeted at Audits of LCEs

63. Various jurisdictional or regional initiatives (herein referred to as jurisdictional initiatives), targeted at audits of less complex (or smaller) entities,¹⁶ have emerged to address challenges when applying the ISAs to audits of LCEs. Other jurisdictions have recently announced commencement of activities to develop a standard(s) or solutions for audits of LCE's within their jurisdictions.¹⁷
64. The LCE Working Group undertook further high-level analysis of these jurisdictional initiatives to gain an understanding of the different approaches taken in the various jurisdictions and determine whether the work done in these jurisdictions may be helpful to the future work of the IAASB. The work undertaken included:
- A desktop review of the requirements and pronouncements in order to understand their main features;

¹⁵ International Standard on Assurance Engagements (ISAE) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*.

¹⁶ These include: the [Nordic Standard for Audits of Small Entities](#) "SASE" (an exposure draft consultation for a proposed standard) developed by the Nordic Federation of Public Accountants, the Sri Lanka Auditing Standard for the Audits of Non-Specified Business Enterprises ("SLAuS") developed at the Institute of Chartered Accountants of Sri Lanka, the Belgium statutory standard for contractual auditing of SMEs and small not-for-profit entities, two [new standards in France](#) for audits that fall below the statutory threshold and an audit standard for small and medium entities, developed based on the IFAC SMP Guide translated into French by the Ordre des Experts Comptables of Morocco.

¹⁷ See [Comment Letter](#) of the Auditing and Assurance Standards Board of the Institute of Chartered Accountants of India (ICAI) and see [Comment Letter](#) of the Institut der Wirtschaftsprüfer in Deutschland e.V. (IDW).

- A comparison to the ISAs of the content relevant to an audit of financial statements;
 - An analysis of how the auditor's opinion is reported, including articulation of the auditor's report and the standard complied with; and
 - Discussions with relevant individuals involved in the development of the initiative in some of the jurisdictions or regions to further understand the context for the initiative and the development process.
65. From the high-level work undertaken, the LCE Working Group's key observations included:
- (a) The jurisdictional initiatives are similar in the following respects:
 - (i) They have been developed using a principles, risk-based approach;
 - (ii) The audit opinion expressed is based on the concept of reasonable assurance. The LCE Working Group has not further analyzed the pronouncements to determine the basis for reasonable assurance within each of the jurisdictions with a relevant pronouncement (i.e., whether the requirements in the jurisdictional initiatives plus other requirements in the jurisdiction provide an appropriate basis for obtaining reasonable assurance). This observation is based on the declarations within each of the relevant pronouncements.
 - (iii) The entities that can be audited under these standards excludes listed companies and those with public accountability.
 - (b) All jurisdictional initiatives are a single standard. Also, all the jurisdictional initiatives considered only the requirements of the ISAs, although some (e.g., the Nordic SASE exposure draft and the Sri Lanka SLAuS standard) also include some key ISA objectives, while none have application or other explanatory material.
 - (c) The jurisdictional initiatives have largely been developed for purposes different to the objective of the IAASB's work in relation to LCEs and with different audiences in mind. For example:
 - (i) The Belgian standard had been developed to address the specific circumstances that only apply to contractual audits in Belgium. Correspondingly, there was a need in Belgium to differentiate an audit under this standard from an ISA audit;
 - (ii) Some jurisdictional initiatives have been developed within the context of the legal and regulatory framework within those jurisdictions (including the Nordic SASE exposure draft). As a result, as certain matters within the ISAs are already covered by local regulation or legislation¹⁸, they have been omitted from the standards resulting from the jurisdictional initiatives.

Within such a specific context, the global replicability of these jurisdictional initiatives would need further modification, and in other cases would not be suitable at all.
 - (d) While all the jurisdictional initiatives make a clear reference to compliance with relevant ethical requirements, only the Nordic SASE exposure draft requires that when applying the proposed

¹⁸ For example, as management acknowledgement of their responsibilities for the financial statements is already prescribed in Nordic legislation, written representation or engagement letter are not required in written form for all audits and apply only in circumstances when these are not clearly defined in applicable laws and regulations.

standard the auditor is required to comply with ISQC 1.¹⁹ Further, none of the jurisdictional initiatives make reference to the ISAs.

- (e) Some of the jurisdictional initiatives include example templates (such as an engagement letter).
- (f) Some of the jurisdictional initiatives include specific guidance within the requirements of the standard (for example, on materiality and considerations for smaller entities in the Sri Lanka SLAuS and Belgium standards).
- (g) In respect of documentation requirements, all jurisdictional initiatives have a general documentation requirement section which varies in length and detail. The Nordic SASE exposure draft also includes additional documentation requirements in each section of the standard (which is consistent in concept with the ISA's detailed documentation requirements within individual standards in addition to ISA 230), while the other jurisdictional initiatives have limited additional documentation requirements within the pronouncements.

Considering the IFRS for SME Standard Approach

- 66. Feedback received from the DP and encouraged the IAASB to draw from the experiences of the IASB while developing the IFRS for SME Standard.
- 67. The IFRS for SME Standard is a self-contained standard (fewer than 250 pages) designed to meet the needs and capabilities of SMEs. The IFRS for SME Standard is aligned with full IFRS standards with modifications based on the needs of users of SME financial statements.
- 68. The IFRS for SME Standard is available for any jurisdiction to adopt, whether or not it has adopted full IFRS standards. The IFRS for SMEs Standard is applicable for entities that do not have “public accountability”. The IASB’s preference is that the Standard is adopted by National Standard Setters without modification, but it understands that, in the context of SMEs, global consistency is less important.
- 69. Compared with the full IFRS suite of standards, the IFRS for SME Standard is less complex in a number of ways:
 - Topics not relevant to SMEs are omitted;
 - Many principles for recognizing and measuring assets, liabilities, income and expenses in IFRS Standards have been simplified;
 - Substantially fewer disclosures are required;
 - The text of full IFRS Standards has been redrafted in “plain English” for easier understandability and translation; and
 - To further reduce the burden for SMEs, revisions are limited to once every three years.

The IASB is currently reviewing this standard and LCE Working Group Staff will monitor the findings from this review.²⁰

¹⁹ International Standards on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*.

²⁰ The deadline for the review is scheduled for end of July 2020. Although not forming part of the development of the specific recommendations for IAASB discussion at the June 2020 IAASB meeting, such findings will help inform the IAASB's future work.

70. The LCE Working Group reflected on the fact that the IASB standard was developed on a topic by topic basis, and set requirements for recognition, measurement, and presentation and disclosure, and that it was relatively uncomplicated²¹ to identify when an accounting standard was relevant or not relevant to an entity, and to scale the level of disclosure requirements. By contrast, an audit is a continuous and iterative process that the ISAs divide into discrete standards, hence the process applied in developing the IFRS for SME standard may be less instructive. However, aspects of the IFRS for SME Standard, in particular in relation to how the standard is used and the entities that may use it, are still relevant.
71. Other aspects noted by the LCE Working Group when the IFRS for SME Standard is applied:
- The basis of preparation for the financial statements requires disclosure be made of this fact, so that users of the financial statements are not misled (the IFRS for SME Standard does not pretend to provide the same level of disclosures as full IFRS standards and users of the financial statements therefore cannot be confused).
 - The needs of users of financial statements can be distinguished between publicly accountable and non-publicly accountable entities. The LCE Working Group reflected that by contrast, the audit standards are different by nature and a reduction in “one aspect” may be harder to achieve while still having the goal of obtaining reasonable assurance.
72. Despite the differences highlighted above, the LCE Working Group believes that learning further from the IASB experiences in developing a separate standard on IFRS for SME is valuable and the LCE Working Group will further engage with the IASB as appropriate, as efforts on exploring a separate standard for audits of LCEs progresses.

Considering Previous Work Undertaken on Behalf of the IAASB

73. In early 2018, an informal working group of the IAASB prepared an example of what a separate standard for an audit of an LCE could look like (i.e., the draft “LCE Specific Standard”). This document was presented as a supplemental document to support the IAASB’s discussions at the March 2018 IAASB meeting (in an Executive Session) in relation to the commencement of IAASB efforts to address the challenges in audits of LCEs. The draft was not specifically discussed as it was provided for reference purposes only to support the discussions.
74. This draft LCE Specific Standard was developed by the informal working group using the Nordic SASE exposure draft as a starting point. To develop the draft LCE Specific Standard the informal working group used the feedback that the Nordic Federation had received on their consultation, including IAASB’s comment letter. In addition, the informal working group reviewed the ISAs in detail and utilized their practical experience as auditors of LCEs in developing the draft. The draft LCE Specific Standard was developed using the same framework as the ISA’s, being consistent with the objectives in the ISA’s and staying as close as possible to the concepts and wording in the ISA’s. As the draft LCE Specific Standard was developed to explore the concept of a separate standard, it includes requirements only (with no application or other explanatory material).
75. The LCE Working Group explored whether this could be used as a basis for further work in developing a separate standard (see paragraphs 79-80 below).

²¹ Although some standards may have been easier than other, there were some on which there were mixed views (for example on hedge accounting).

Other Matters

76. The LCE Working Group also deliberated on a number of issues that would need to be considered going forward that are relevant for the development of a separate standard:

- (a) A number of respondents to the DP expressed views that an appropriate approach would be to first develop a separate standard for audits of LCEs, and then as a second step, and through a plan of convergence, start revising the ISAs using the separate standard as a basis for the revision. The two workstream plan being presented in this paper address the concerns encompassed in these suggestions from respondents, but the workstreams are more distinct and are meant to run concurrently rather than consecutively. Furthermore, the intention would be that both workstreams inform each other (i.e., neither would be done in isolation).
- (b) In relation to the types of entities for which a separate standard may be appropriate (i.e., describing an “LCE” for the purpose of what type of entity a separate standard would be appropriately used for), respondents to the DP indicated that further consideration should be provided with respect to the following:
 - (i) Given that both large and small entities can be complex, it is important that the LCE definition (description) avoids any ambiguity, and excludes from its scope entities listed in regulated markets or those who have issued public debt;
 - (ii) The definition (description) of LCEs should provide adequate consideration for entities classified as Public Interest Entities (PIEs) as defined by the International Ethics Board for Accountants’ (IESBA) Code of Ethics, and national regulations, including unlisted banks and insurers, entities receiving a significant portion of its income from public sources, charities, or entities raising crowdfunding, given that such entities tend to have greater public accountability and carry a higher overall risk;
 - (iii) Given that LCEs may be a component of a more complex group or PIEs, the definition should provide sufficient clarity as to how it is applied to the audit of the separate entities forming part of a group; and
 - (iv) The present definition (description) (i.e., in the DP) of an LCE does not provide sufficient considerations relevant for non-for-profit organizations and public sector entities.

The LCE Working Group briefly discussed the scope of a separate standard, including arguments for and against prescriptively determining the suitability of the standard for certain types of entities (for example, not being suitable for listed entities or for entities with public accountability). In the analysis of the jurisdictional initiatives on a separate standard it was noted that listed entities had been specifically excluded.

77. Other matters the LCE Working Group identified that will need further consideration if the work on a separate standard progress include:

- The relationship between the requirements of such a separate standard and the inclusion of any application material, as well as the applicability of ISA 200, in particular the requirements of ISA 200, paragraph 19²²;

²² ISA 200, paragraph 19 requires the auditor to have an understanding of the entire text of an ISA, including its application and other explanatory material, to understand its objectives, and to apply its requirements properly.

- Guidance materials that may be needed to support the effective implementation of such a separate standard (not necessarily for the IAASB to develop but working or coordinating with others to ensure that there is adequate implementation support when implementing and using the separate standard).
 - How the audit opinion paragraph of such a separate standard would be presented; and
 - The “placement” of such a separate standard within the overall ISAs structure.
78. Additional work undertaken by IAASB Staff in relation to the LCE Specific Standard consisted of:
- A high-level mapping²³ of the content of the LCE Specific Standard to the ISAs; and
 - A detailed mapping of the objective and requirements of the LCE Specific Standard related to planning to the objective and requirements of ISA 300, *Planning an Audit of Financial Statements* to illustrate an example of how one standard could be developed as part of a separate standard.

Supplements C and D provide further details which demonstrate the mapping of the LCE Specific Standard to the ISAs (content and the planning requirements).

Working Group’s Observations

79. The LCE Working Group’s key observations from the work undertaken included the following:
- (a) The LCE Specific Standard follows a structure that is aligned more to the ‘process’ of an audit, while the individual ISAs are focused on specific topics (i.e., written in a linear way not necessarily following the process of an audit). Notwithstanding the different format of the standards, the majority of the ISAs can be mapped into the structure of the LCE Specific Standard, with a few exceptions (e.g., ISA 600²⁴, ISA 701²⁵, and other standards which may not be relevant for LCEs).
 - (b) The LCE Working Group notes that if the LCE Specific Standard approach is used as a basis for its future work, further thinking will be required to allow for conditions that can “loop-back” into the requirements of ISAs for areas not covered by the separate standard.
 - (c) The LCE Working Group believes that the LCE Specific Standard is a good starting point for further work to develop a separate standard. However, further work will be required on the content and also to update the standard with recent changes to the ISAs to bring the requirements up to date. Further work will also be required to map all the requirements within the separate standard back to the relevant ISAs to ensure completeness, while also ensuring the separate standard maintains the same robustness of the ISAs.
80. The expected timing of the development of a separate standard is 3-4 years based on the normal due process steps (as set out in paragraph 11). This estimated timing is based on a presumption that the work already undertaken by the informal IAASB working group is used, and that there are no

²³ The high-level mapping has been performed based on the overall content covered by the LCE Specific Standard and has not entailed further detailed work on the requirements.

²⁴ ISA 600, *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)*.

²⁵ ISA 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*.

unexpected circumstances during the development of a separate standard, in which case the time period would likely extend.

In Summary – Separate Standard Workstream

In considering all of the relevant matters related to exploring the development of a separate standard as set out in this paper, the LCE Working Group would like to develop the specific recommendations for development of a separate standard by using the work that has already been done on the LCE Specific Standard (see paragraphs 78–80 above). In the view of the LCE Working Group this would expedite the process for the development of a separate new standard and would leverage the thinking that has already been done. The LCE Working Group is planning to put forward in June 2020 recommendations that would detail the basis on which a separate standard would be developed (subject to Board agreement to this workstream) and would also highlight the many areas where further consideration is needed.

Matters for IAASB Consideration

2. The IAASB is asked for its views on a Separate Standard Workstream on the basis of the LCE Working Group's views on the possible development of a separate standard for LCEs as set out in Section III above, i.e. by using the LCE Specific Standard as a starting point.
3. If a separate standard were to be developed, the IAASB is asked for its views about the applicability of such a standard, i.e., should certain entities (e.g., listed or those with a public interest nature) be explicitly scoped out?
4. The IAASB is asked whether there are any other matters that should be considered by the LCE Working Group in its development of recommendations relating to the Separate Standard Workstream?

IV. Other Matters Relevant to the ISAs

Aspects of the ISAs that Have Been Specifically Identified as an Issue or Challenging to Implement

81. The responses to the DP identified a number of specific areas within the ISAs that are challenging to implement or are issues when undertaking audits of LCEs (as outlined in [Supplement A to Agenda Item 6](#)). The LCE Working Group acknowledges that each of these specific issues would need to be further considered to determine whether there is a focused action(s) (or otherwise) that can be undertaken by the IAASB to address the issue. This may include:
 - Development of a Questions and Answers (Q&A) (or other non-authoritative material) that may help clarify the application of a particular requirement.
 - Consideration of a narrow scope amendment²⁶ to the ISA to address the issue.
 - Coordinating with others (such as national standard setters (NSS) or IFAC) to address the issue.
82. In deliberating whether specific issues and concerns raised could be addressed through targeted changes,²⁶ the LCE Working group considered the feasibility of making such changes in relation to the

²⁶ The IAASB's newly approved Strategy for 2020–2023 and Work Plan for 2020–2021 contemplates further consideration about the introduction of 'narrow scope amendments' into the IAASB's 'suite of tools.' Consideration will be given during 2020 to whether these could be effectively used, and how they would operate (i.e., associated due process).

standards that were analyzed for the purpose of determining the feasibility of developing a “building-blocks approach” (as discussed in Section II).

83. **Supplement A** (which illustrates the LCE Working Group's views about developing a “building-blocks approach”) also illustrates examples of specific issues or concerns that have been raised by respondents to the DP in relation to ISA 300. With the exception of the issues related to documentation (as explained in paragraph 84 below), the LCE Working Group came to the conclusion that most of these specific areas would be better dealt with in explanatory material or other non-authoritative material rather than making targeted changes to the requirements. However, this analysis was only performed with regard to ISA 300 and would need to be performed for all of the matters identified to determine whether there are some other focused, shorter-term solutions. Such work could form part of the ISA Focused Workstream.
84. Issues in relation to the documentation requirements within the ISAs was a common theme in many of the responses to the DP. Respondents highlighted that the requirements related to documentation (in ISA 230 as well as the documentation requirements within the individual ISAs) are disproportionate for LCEs, and, in this context, do not add value or enhance audit quality. It was noted that it can be burdensome to go through a process of elimination to determine which requirements do not apply, as well as to document why they may not be applicable. Respondents also noted that documentation requirements were becoming increasingly onerous, especially within the specific ISAs covering the planning and completion stages of the audit. Respondents expressed views that further clarity and guidance through examples would be helpful to show the variability in levels of documentation based on the level of complexity within the entity.
85. Accordingly, the LCE Working Group is of the view, that as part of the work undertaken to revise the ISAs in the ISA Focused Workstream, that specific work be undertaken to determine how to best address the many issues and challenges that relate to documentation. This will include, for example, consideration of any inconsistencies in the way that the documentation requirements are presented within each standard, clarifying how ISA 230 is intended to be implemented, and whether other changes are needed to help alleviate some of the challenges with regard to documentation.

Enhanced Accessibility of the ISAs

86. IAASB Staff, in collaboration with IFAC, have commenced work to convert the IAASB's Handbook into an electronic format. The LCE Working Group discussed various attributes that would be helpful within an electronic version of the Handbook (such as enhanced search functionality, the ability to bookmark pages, providing links between definitions, requirements and application material, etc.), and these suggestions will help inform the initial scoping of the work to convert the Handbook. It is also intended that further consideration will be given to the impact on both workstreams of the ability of an electronic Handbook to address some of the issues and challenges identified, as well as whether any of the work done in these workstreams may also inform the functionality of a future electronic Handbook.

Reviewing how Different Methodologies Address Audits of LCEs

87. Respondents to the DP indicated that guidance within methodologies have proved to have some success in assisting engagement teams in managing some of the challenges relating to audit work for smaller entities. The LCE Working Group therefore plans to further understand the nature and extent of this guidance to determine whether it can help inform the IAASB's work efforts in this area. This could be done through further understanding various methodologies and related guidance being used for audits of smaller entities, such as those used by Big 4 accounting firms.

Coordinating with Others

88. The LCE Working Group discussed the importance of coordinating with others within the scope of this project, such as NSS and IFAC (in relation to the two proposed workstreams, as appropriate), and encouraging others to act on relevant topics at the jurisdictional level (for example, policy decisions, and topics such as the value of audit²⁷ and commercial considerations to audits of LCEs).²⁸

LCE Working Group Future Actions

89. The LCE Working Group and Staff have also identified the following areas which have not yet been addressed, but for which action or further consideration is still planned:
- (a) Further consider the description of “less complex entities”. Taking into account the description within the DP and respondents’ comments thereto. Although this will directly impact the Separate Standard Workstream (i.e., will influence those entities for which the separate standard was developed) it is still applicable more generally as a term used in our literature.
 - (b) Understand the work being undertaken by NSS with regard to solutions for LCE audits (for example, connect with AICPA on the dynamic audit solution (DAS) project); and
 - (c) Analyze the specific issues noted by respondents with regard to complexity, readability, understandability, scalability and proportionality of the ISAs so as to identify “pass-on” items (including areas where examples could be helpful) with regard to other IAASB ongoing projects.

Matters for IAASB Consideration

5. Does the IAASB have any observations and comments pertaining to the other matters, including whether there are any further actions to be pursued by the LCE Working Group?

²⁷ IFAC have recently issued a point of view (POV) on “High Quality Audits: (<https://www.ifac.org/what-we-do/speak-out-global-voice/points-view/achieving-high-quality-audits>).

²⁸ Further consideration may be given to how the IAASB can work with others on these matters (as appropriate) (for example with NSS through discussions at the May 2020 NSS meeting or the 2021 third conference on LCEs supported by the French profession).

Appendix 1

Draft Minutes²⁹ from the December 2019 IAASB Discussions Audits of Less Complex Entities (LCEs)

Professor Roger Simnett, Chair of the LCE Working Group presented a summary of the respondents' feedback on the Discussion Paper (DP),³⁰ and other related outreach, as included in **Agenda Items 6, 6-A and 6-B.1 – B.11**.

The following sets out the more substantive comments from the Board on the presented agenda items.

SUMMARY OF RESPONDENTS' FEEDBACK

The Board acknowledged the significant interest and support for the IAASB work in the area of LCEs, noting the substantial number of responses received from a broad range of stakeholders and from various regions and also acknowledged the thoroughness of the analysis of the respondents' feedback as provided in **Agenda Item 6**.

The Board broadly supported the LCE Working Group proposed direction for future work by the IAASB to respond to the input relating to audits of LCEs, including an LCE and ISA focused workstream, and asked the LCE Working Group to further explore the possible activities under both workstreams as they continue further information gathering activities through to June 2020. With respect to the respondents' feedback, the Board asked the LCE Working Group to:

- Consider the scope of the entities that should form part of the LCE description, especially with regard to listed entities and entities with a degree of public accountability, as well as providing further thought on the risk-based factors that could be considered in the LCE description. Concern was expressed that should separate requirements for LCEs be further explored as a proposed action, then such requirements should not extend to listed and public interest entities.
- Further analyze the root causes related to the challenges with ISAs in audits of LCEs and especially in respect of the audit procedures deemed to add no or little value.
- Clarify how technology can be utilized to address some of the challenges with ISAs in all audits, including audits of LCEs.
- Explore the feasibility of a "building-blocks approach" to revising the ISAs and the relationship between such an approach relative to scalability issues within the ISAs as informed by respondents' feedback to the DP.
- Revisit the role that IAASB could play while encouraging others to act on topics such as the value of audit, and the commercial considerations to audits of LCEs.

FEEDBACK STATEMENT

The IAASB agreed that it was important to keep stakeholders informed of its progress in relation to audits of LCEs. Accordingly, it was agreed that the Feedback Statement as presented in **Agenda Item 6-A** be published mid December 2019 detailing what the IAASB has heard from the consultation, subject to a few editorial and other Board comments.

²⁹ These draft minutes are still subject to review by the IAASB and therefore further changes may be made.

³⁰ <https://www.iaasb.org/publications-resources/discussion-paper-audits-less-complex-entities>.

IAASB CAG CHAIR'S REMARKS

Mr. Dalkin confirmed the support of the CAG for continued work in the area of LCEs and encouraged further exploration of the feedback received to date.

PIOB OBSERVER REMARKS

Prof. Van Hulle expressed the PIOB support for this IAASB activity and emphasized that it will be important to fully analyze and understand the root causes of the challenges when applying ISAs to audits of LCEs. Further, while the IAASB is developing solutions in this area, there should be close cooperation and coordination with National Standard Setters (NSS).

WAY FORWARD

The LCE Working Group will continue to analyze the feedback from stakeholders to help determine the way forward. Further information gathering activities will continue until June 2020, at which time it is anticipated that a decision about the way forward will be made.

LCE Working Group and Outreach

LCE Working Group Members

1. The LCE Working Group consists of the following members:

- Roger Simnett (Chair)
- Isabelle Tracq-Sengeissen (assisted by Fabien Cerutti)
- Kai Morten Hagen
- Chun Wee Chiew
- Rich Sharko
- Brendan Murtagh
- Gordon Cummings
- Christopher Arnold

Further information about the project can be found [here](#).

Working Group Activities since the March 2019 IAASB Discussion

2. The LCE Working Group met once in person (October 2019) and held one teleconference (November 2019) since the last IAASB discussion in March 2019.

Working Group Outreach

In January 2020, LCE Working Group representatives, including the LCE Working Group Chair, and IAASB Staff, met with representatives from the Thai auditing profession and Thai Securities Exchange (SEC) to discuss matters related to challenges when applying the ISAs. The outreach also included an event supported by the Thai SEC with approximately 250 participants, including directors, audit committee members, preparers, firms, practitioners and others, to present on IAASB projects, with a focus on audits of LCEs.

In February 2020, the LCE Working Group Chair presented at the Audit and Assurance for Listed and Non-Listed Entities Conference (ALLNEC) hosted by Deakin Business School, Department of Accounting and the Auditing Special Interest Group (ASIG) of the British Accounting and Finance Association (BAFA) on the challenges in the auditing of SMEs. This event convened academics and non-academic delegates representing the international auditing academia, accounting professionals in practice and in business and standard setters and regulatory bodies.

In February 2020, the IAASB Chair and Technical Director met with stakeholders representing auditors of small- and medium-sized entities (SMEs) in Germany and France. The various representatives were supportive of the IAASB's efforts with regard to the project on Audits of LCEs. It was noted that the ideal solution would be to revise the ISAs, but there was recognition that this is not a realistic solution in the shorter term. It was emphasized that there needed to be a more immediate (preferably global) solution. There was also discussion about the different initiatives in these jurisdictions about what was being done to address the needs of their stakeholders in these regions.