

Supplement 2-06 to Agenda Item 6

Audits of Less Complex Entities – ED-ISA for LCE – Q3(b) Views are sought on the Authority (or scope) of ED-ISA for LCE (Part A of the proposed standard). In particular: Are there unintended consequences that could arise that the IAASB has not yet considered?

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\1) No

3. Regulators and Audit Oversight Authorities

Botswana Accountancy Oversight Authority

None noted.

4. National Auditing Standard Setters

Public Accountants and Auditors Board Zimbabwe

No noted

5. Accounting Firms

Crowe Global

We do not consider that they are any unintended consequences.

Famme & Co. Professional Corporation

Nothing to note.

6. Public Sector Organizations

Audit Scotland

No.

Auditor-General of New Zealand

We do not foresee any unintended consequences arising from the scope of the proposed standard.

Government Accountability Office (USA)

We are not aware of any unintended consequences that may arise that IAASB has not considered.

7. Professional Accountancy and Other Professional Organizations

Botswana Institute of Chartered Accountants

None noted.

Chartered Governance and Accountancy Institute in Zimbabwe

We believe that there are no unintended consequences that could arise that the IAASB has not yet considered.

European Federation of Accountants and Auditors for SMEs

We are not aware of any unintended consequences that could arise.

Indonesian Committee on Public Accountant Profession (KPAP)

We believe all unintended consequences that could arise have been addressed in the proposed standard.

Institute of Certified Public Accountants of Kenya

None.

Institute of Certified Public Accountants of Rwanda

There are no unintended consequences that we can foresee.

Institute of Chartered Accountants of Ghana

we cannot think of any unintended consequences that could arise that the IAASB has not yet considered.

Institute of Chartered Accountants of Jamaica

None Noted

Instituto Mexicano de Contadores Públicos (IMCP)

Nothing additional identified or that we consider could have an impact in our jurisdiction.

REA Auditores

We are not aware of any unintended consequences that could arise.

Society of Certified Accountants and Auditors of Kosovo (SCAAK)

We are not aware of any unintended consequences that could arise.

Wirtschaftsprüferkammer (WPK)

We currently do not see any.

8. Academics

Argentine institute of Auditing Professors

We have not observed any unintended consequences that have not been contemplated in this ED.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2a) Inconsistency In Application\Inconsistency between Jurisdictions

3. Regulators and Audit Oversight Authorities

Canadian Public Accountability Board

Different firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities with similar characteristics. This may contribute to confusion for users of the financial statements and undermine the objective of achieving global consistency.

Irish Auditing and Accounting Supervisory Authority

The scope of the ISA for LCE is subjective and likely to lead to inconsistent use of the standard. The provisions contained in the exposure draft leave room for the auditor to evaluate whether the standard is applicable to an audit, and this could lead to situations where different auditors, firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities that exhibit similar characteristics. This may contribute to confusion for users of financial statements and undermine the objective of achieving global consistency.

National Association of State Boards of Accountancy (NASBA)

A stated reason for the separate standard for LCEs is that a global solution is preferable to increasingly fragmented solutions. However, the Authority guidance seems to embrace the possibility that jurisdictions will modify the proposed standard and put their own versions into practice. This would ultimately result in various national standards instead of the desired global standards.

4. National Auditing Standard Setters

Institut der Wirtschaftsprüfer in Deutschland e.V. (IDW)

One of the issues that may arise is that there may be pressure on local authorities or standard setters to not restrict the application of the LCE standard beyond those restrictions already set forth in the Authority. Given the views we express in (a) above in relation to implementability, it may therefore be helpful if the IAASB expresses in the Authority the IAASB's expectation that local authorities or standard setters will provide additional requirements and guidance on scope as described in the examples of jurisdictional determination of the Supplemental Guidance for the Authority of the [Draft] Standard.

Royal Netherlands Institute of Chartered Accountants (NBA)

We foresee juridical and jurisdictional challenges. It is difficult to define which entities are LCEs as the definition is subjective and leaves room for interpretation. Competent authorities might also struggle with this and may not allow this proposed standard to be used for statutory audits. If the standard will not be applicable in various situations, the added value seems limited. Within our mandate -which excludes statutory audits- we will not implement this LCE Standard considering these issues.

5. Accounting Firms

BDO International

Finally, the expectation for legislative or regulatory authorities or relevant local bodies with standard-setting authority to issue provisions and accompanying guidance for adoption and implementation of the LCE standard may not be welcomed by all jurisdictions. For those local bodies that do issue local requirements and guidance, there is a risk of inconsistent work effort and documentation across different jurisdictions, although it is beyond the mandate of the IAASB to resolve inconsistencies arising from local standards and regulations.

Mazars

Yes, we believe there are potential unintended consequences that could detract from a high quality ISA for LCE audit and thus not be in the public interest as follows:

Has there been an analysis of the impacts if some jurisdictions refuse to adopt it, especially some those with a strong voice in the international debate?

Moore Global Network Limited

Our biggest concern, as a global network, is that as things stand there may be jurisdictions which do not adopt or allow the use of the LCE standard. This will threaten engagement performance consistency and thus quality. We strongly believe that IAASB should take some time to consider how to avoid or mitigate this threat.

7. Professional Accountancy and Other Professional Organizations

ASSIREVI

There could be an issue with the potential inconsistent application of the Authority in the long term that could prevent the use of ED-ISA for LCE or trigger its discontinuation depending on the entity's qualitative characteristics. We believe that, over time, the existence of auditors specialised in the audit of LCEs and, therefore, with less expertise with the ISAs, could imply that these auditors would not have all the knowledge necessary to appropriately evaluate the qualitative characteristics. This would increase the risk of the inappropriate application of ED-ISA for LCE.

Belgian Institute of Registered Auditors (IBR-IRE)

There is a broad definition of what "complex" encompasses. In addition, interpretation of the definition is quite subjective which - in the end - could lead to the proposed standard not likely to be used that often as it might be intended by the IAASB. If the interpretation of the word "complex" and the scope of the standard is defined in every country in a different way, the standard will lose its added value.

Confederation of Swedish Enterprise

We believe that one consequence of letting firm policies or procedures decide if ISA for LCE should be applied or not is that it might have an impact on international/global level. If a global audit firm prohibits the use of ISA for LCE generally, for whatever reason, this might have a huge impact on the application of the standard.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2a) Inconsistency In Application\Inconsistency in Application (General)

1. Monitoring Group

International Forum of Independent Audit Regulators (IFIAR)

The provisions contained in the exposure draft leave room for the auditor to evaluate whether the standard is applicable to an audit, and this could lead to situations where different auditors, firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities that exhibit similar characteristics. This may contribute to confusion for users of the financial statements and undermine the objective of achieving global consistency.

3. Regulators and Audit Oversight Authorities

Canadian Public Accountability Board

Unintended consequences of a separate ISA for LCE standard

Different firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities with similar characteristics. This may contribute to confusion for users of the financial statements and undermine the objective of achieving global consistency.

Irish Auditing and Accounting Supervisory Authority

The scope of the ISA for LCE is subjective and likely to lead to inconsistent use of the standard. The provisions contained in the exposure draft leave room for the auditor to evaluate whether the standard is applicable to an audit, and this could lead to situations where different auditors, firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities that exhibit similar characteristics. This may contribute to confusion for users of financial statements and undermine the objective of achieving global consistency.

4. National Auditing Standard Setters

Australian Auditing and Assurance Standards Board

There were also concerns that the high level of subjectivity included in the different qualitative characteristics which currently govern the use of the proposed standard may lead to inconsistent application in practice and unintentionally undermine the confidence users have on LCE audits.

Indonesian Institute of Certified Public Accountants (IAPI)

Significant judgement will rest with the firms and engagement teams in interpreting whether entities fall within categories of entities meeting the definition of LCE. There will be a potential risk of inconsistency in the judgement made.

Malaysian Institute of Accountants

Due to understandably different territory limitations on the use of the proposed standard, there may not be a universal application of this standard internationally which may add to the confusion in the market especially if the other regions/countries as identified in the ED ends up going ahead with their country specific version of an LCE standard.

New Zealand Auditing and Assurance Standards Board

Applying the QCs in conjunction with the concept of 'if in doubt, you are out' should mean that auditors come to the same conclusion as to whether the LCE standard can be applied.

However, the extent of judgement involved in the consideration of the QCs by the firm or at the engagement level in the scoping of the standard might create inconsistency in practice whereby different auditors may arrive at different conclusions as to whether the same entity could qualify as an LCE.

5. Accounting Firms

Duncan & Toplis Limited

Please see (a), the subjective nature of qualitative characteristics may lead to international divergence.

Ernst & Young Global Limited

Consideration of qualitative characteristics by firms and practitioners may lead to unintended inconsistencies across the profession on the use of the proposed standard since these are only expected to be indicators of matters or circumstances that are deemed complex. The use of professional judgment will be required to evaluate the qualitative characteristics, and this will inherently result in inconsistencies of use across the profession because each characteristic is subject to interpretation.

We believe that the consideration of qualitative characteristics by firms and practitioners may lead to unintended inconsistencies across the profession on the use of the proposed standard since these are only expected to be indicators of matters or circumstances that are deemed complex. The use of professional judgment will be required to evaluate the qualitative characteristics, and this will inherently result in inconsistencies of use across the profession because each characteristic is subject to interpretation.

HLB International

There might be instances where two auditors come to different conclusions regarding the complexity assessment for the same entity and this might confuse entity's management, users and the regulators. It should be emphasised that existence of qualitative characteristics may not give rise to complexity on its own

and the aggregate impact of the characteristics should be considered by the auditor when deciding on the appropriateness of ED-ISA for LCE.

PKF International Limited

In our view, the judgements needed to apply the qualitative characteristics, as set out in the Authority, will lead to inconsistencies in application among users of the proposed standard. To help reduce this risk, the IAASB could consider a longer list of prohibitions and reduce the list of qualitative characteristics.

In developing a longer list of prohibitions, we recommend that the IAASB also consider criteria that go beyond the complexity associated with the entity to recognise that the wider complexities affecting an audit engagement can arise from the broader nature of the engagement itself (as we have suggested elsewhere within this response).

PriceWaterhouseCoopers

We believe there are two specific unintended consequences that could result from the proposed approach to drafting of the Authority section that the Board needs to reconsider:

As noted in our response to part (a), the potential to apply the standard on larger private entities may result in risks to audit quality if the work effort that would result from applying the standard is not deemed commensurate with the nature and circumstances of the entity and its operations. Further, the level of subjectivity in the Authority will likely lead to inconsistency in the appropriate use of ISA for LCE versus the ISAs in similar fact patterns, which would be undesirable from an audit quality and comparability perspective (including potential confusion from users of the financial statements with regard to the level of audit work performed on audits of similar entities). Audit inspection findings are not limited solely to listed and PIE audits and maintaining appropriate safeguards to quality in all segments of the audit market, including audits of medium/large private entities, is important. As we note in our response to question 1, we believe the ISAs remain the appropriate benchmark for audits in this segment of the audit market.

The ISAs set out an appropriate basis for delivering a high-quality reasonable assurance audit that, in our view, should represent the presumptive basis for an audit of financial statements. We believe the manner in which the scope and authority of the proposed ISA for LCE has been defined undermines this presumption. As drafted, it sets an expectation that the LCE standard can be used for any audit unless the auditor determines that complexity exists. We believe that the opposite should hold true: an audit should be conducted in accordance with the ISAs unless the auditor determines that the specific criteria for use of the LCE standard can be met. This would serve to protect the primacy of the ISAs as the “default” global auditing standards. As such, we recommend revising the qualitative characteristics to focus on the characteristics that are indicative of an LCE and that, when exhibited, would make the standard appropriate for use. We describe these changes in our response to question 4(b).

7. Professional Accountancy and Other Professional Organizations

Institute for the Accountancy Profession in Sweden (FAR)

For the qualitative characteristics the auditor is expected to use professional judgement. Most entities will probably be rather clear to assess whether they are LCE or not. However, there might be instances where two auditors come to different conclusions regarding the complexity assessment. In rare situations this might confuse clients and the regulators.

If firms or networks decide not to allow the use of the standard this might confuse stakeholders and impair the public interest’s understanding of the standard.

Korean Institute of Certified Public Accountants

However, the prevailing view among domestic stakeholders is that significant level of judgment is likely to be involved in determining whether the ISA for LCE is appropriate to use because the qualitative characteristics described in paragraphs A.8 - A.9 are still abstract. Exercising a significant level of judgment in determining whether an entity is an LCE or not may cause problems as below.

Different engagement teams may make different judgements about similar situations, which leads to confusion. For example, if an engagement partner or auditor is replaced, the incoming partner or auditor may make a different judgement about the same situation.

Malta Institute of Accountants

Significant judgement will rest with firms and engagement teams in interpreting whether entities fall within such categories. The potential for inconsistency in judgement will be significant.

Ordre National des Experts Comptables et des Comptables Agréés du Burkina Faso (ONECCA-BF)

The Qualitative Characteristics provide a second step in determining when it would be inappropriate for an audit of financial statements of an entity to be undertaken using the proposed standard, once it has been determined that the audit engagement is not prohibited from use of the proposed standard as set out in paragraph A7.

The Qualitative Characteristics set out in paragraph A9 of the proposed standard of (i) business activities, (ii) organizational structure, (iii) ownership, (iv) oversight, (v) regulation, etc. are effective indicators against which to measure whether an entity is an LCE.

However, as drafted, these Qualitative Characteristics require the auditor to exercise professional judgment because of the use of words such as “complex”/“complexity” and “not...simple”. The use of professional judgment by auditors can lead to the inconsistent and inappropriate use of the proposed standard. There should be little room for the exercise of professional judgment. It is our view that the required use of professional judgment is too high and that a higher level of prescription is more desirable.

Paragraph A9 of the proposed standard uses the words “complex”/“complexity” nine times and “not...simple” once. Different auditors have different definitions of complexity and simplicity. For example, the use of a Black Scholes method in calculating an accounting estimate may be complex to one auditor but simple to another, depending on, perhaps, how often the auditor has audited such an accounting estimate in the past. As such, the auditor who believes that such an accounting estimate is simple, would choose to use the proposed standard, but the auditor who believes that the accounting estimate is complex, would be precluded from using the proposed standard.

This simple example illustrates how the professional judgment of an auditor can lead to the inconsistent and inappropriate use of the proposed standard.

Polish Chamber of Statutory Auditors Warsaw (Regional Branch)

Response: The description of the qualitative characteristics relating to the limitation of the applicability of the standard is imprecise and may lead to extreme differences in interpreting the scope of units for which the standard will be applied.

Excluding the possibility of applying the standard to aggregated reports (being the total of the entity's financial statements and all of its branches [business units]) should be considered.

South African Institute of Professional Accountants

We have a concern regarding the level of professional judgement required together with the understanding of the term complex transactions. This could lead to inconsistent application between auditors on very similar organisations.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2b) Burdensome or Hard to Implement\Need to Transition

3. Regulators and Audit Oversight Authorities

Canadian Public Accountability Board

Switching to the ISAs partway through an audit when unforeseen circumstances arise may take longer than if the ISAs were applied from the start with no additional benefit. This will also add complexity for private

companies audited using the ISA for LCE who later become public and may need to transition to the ISAs for multiple years.

National Association of State Boards of Accountancy (NASBA)

Finally, with respect to the Authority, we are concerned about the potential for situations in which a practitioner initiates an audit under the LCE standards and then discovers a fact that disqualifies the engagement from further use of the LCE standards. The Exposure Draft directs the practitioner to then follow the full ISAs. At a minimum, such occurrences could be disruptive to the audit process and adversely impact the auditors, the auditees, and the users of the financial statements. Beyond that, it begs the question of what the auditor's report will state in terms of the standards followed. We believe more guidance should be provided on those considerations and what the audit report would state about what standards were followed.

4. National Auditing Standard Setters

Australian Auditing and Assurance Standards Board

While the IAASB may not expect transitioning between the proposed LCE standard and the full suite of ISAs to occur frequently, Australian stakeholders took the view this scenario may often occur, considering the judgement involved in applying the qualitative characteristics in deciding to apply the standard particularly with reference to new engagements. Our AUASB stakeholders considered that transitioning to the full suite of ISAs mid-way through an engagement would be an onerous task, and consequently practitioners may opt to not use the standard in the first place. The AUASB considers that more flexibility in the transitioning provisions of the proposed ED-ISA for LCE Standard is necessary to avoid this being a barrier for practitioners to use the proposed standard. For example, in scenarios where an LCE audit has a one-off complex matter in a particular reporting period, it's logical to refer to the more detailed requirements within a specific relevant ISA and 'top-up' the audit requirements for such an engagement, rather than having to start that audit again using the full suite of ISAs. This could also apply to more than one complex matter triggering reversion to specific ISAs.

New Zealand Auditing and Assurance Standards Board

Alternatively, given that there are many specific prohibitions and QC considerations, it may be deemed safer to apply the full ISAs than risk having to transition to full ISAs mid-way through the audit. Auditors may naturally default to over auditing in order to minimise their liability risk. This reduces the attractiveness of the standard.

5. Accounting Firms

BDO International

The requirement to transition to a 'full ISA' audit if there is a change in qualitative characteristics (i.e., primarily the discovery of an estimate with high estimation uncertainty) is a fatal flaw that will prevent adoption of the LCE standard. It is not practical to switch the auditing framework mid-way through the audit when the auditor could simply refer to ISA requirements and guidance needed to address the issue. Auditors should not be penalized for going above the minimum requirements of the LCE standard. From a public interest perspective, and mindful of the need to maintain audit quality, under any framework (accounting or auditing), auditors should be able to go beyond the minimum requirements and still report under the stated framework. As most auditors will likely also do some 'full ISA' audits, they will have knowledge of those standards that they cannot 'turn off' when doing an LCE audit. It will be very difficult to stop those auditors from going beyond the LCE standard when performing LCE engagements. Going above the minimum requirements of the LCE standard should not be mentioned in the auditor's report via references to those ISAs.

Grant Thornton International Limited

As noted above, allowing modification at the firm and the engagement level can only result in inconsistent application of the standard. In particular, in this respect, we would highlight using the qualitative criteria of accounting estimates. This could have the following consequences:

Based on an initial understanding of the entity, no accounting estimates are identified that meet the prohibition criteria. As the auditor continues with the audit under ED-ISA for LCE and obtains an understanding of the entity and its environment, an accounting estimate is identified that makes the use of ED-ISA for LCE prohibited. The auditor then has to switch to the ISAs mid-audit.

The auditor commences the audit under ED-ISA for LCE, performs planning, risk assessment and some interim audit procedures. Shortly before the period end, the entity enters into a complex financing arrangement, or acquires a new subsidiary. The auditor is no longer able to use ED-ISA for LCE and has to switch to the ISAs after performing a significant amount of work under ED-ISA for LCE.

In the first year ED-ISA for LCE is effective, the entity qualifies to be audited under the Proposed Standard. In year two, the environment in which the entity operates changes, making use of ED-ISA for LCE prohibited, the auditor therefore performs the audit under the ISAs in that year. In year three, the factors that caused the change in the environment no longer exist and the entity qualifies to be audited under ED-ISA for LCE again. The audit is therefore not being performed under consistent auditing standards.

We are of the view that repeated change in the standards under which an entity is audited would make ED-ISA for LCE undesirable to firms and to users of the auditor's reports. Potentially, firms may find it necessary to develop and maintain at least two methodologies to be prepared for the need to audit under the ISAs; and users would likely not understand why an audit report indicated it was prepared in accordance with the ISAs in one year and ED-ISA for LCE in another year.

KPMG IFRG Limited

We note that the definitions set out in the authority section focus on characteristics of the entity, however, situations may arise that are not entity-specific matters and which are not within the control of the entity. For example, a matter may be related to the entity's environment, e.g., an entity may have relatively simple estimates in most years, but during times of economic uncertainty/ volatility, e.g. as a result of the COVID-19 pandemic, complexity may be introduced to the estimation process. Such an entity may therefore meet the criteria to be an LCE in some years, but not in others, which would not be a desirable outcome and could place entities and auditors under significant pressure in terms of additional work needed to transition in and out of the LCE ISA over time.

6. Public Sector Organizations

Australian Council of Auditors General

Most ACAG offices will have LCE within their audit portfolio. However, public sector entities are inherently subject to once-off complex transactions, often with little notice. Significant audit effort could be expended applying the ED LCE only to determine at a late stage that additional ASAs require application.

7. Professional Accountancy and Other Professional Organizations

Federation of Accounting Professions of Thailand

The confusions/complications between the audits of the same entity when the status of LCE may change to non-LCE and back to LCE over years. IAASB should consider providing more detailed guidance of when there are changes in the status of LCE, as it will cause a burden and difficulty on both entity being audited and the auditor.

Institute of Chartered Accountants of Pakistan

We believe that transition from ISA for LCE to ISAs could become relevant and necessary in certain circumstances. For example, this would be necessitated when during the audit it is discovered that ISA for LCE is not appropriate because of complexity of entity's transactions and operations, and the auditor is required to transit and perform the audit in accordance with ISAs.

We understand that the proposed ISA for LCE does not discuss the practical aspect of transitioning. From practical side, transitioning from ISA for LCE to ISAs would generally require more audit efforts. There could be disputes between auditor and engaging party regarding increased time and effort and commercial considerations relating to audit fees. A delay in audit completion due to changed scope (i.e. from ISA for LCE to ISAs) may not result in cost effective audit. These potential challenges may deter auditors from electing and using the proposed standard for less complex audit clients.

International Federation of Accountants' Small and Medium Practices Advisory Groups

We also believe that in cases where an auditor changes their decision to move into the Audits of LCEs from the full ISAs or back to the full ISAs as audit work progresses, this should not reflect negatively on their client acceptance and continuance process, nor should this result in any additional documentation requirements.

There is one issue that could be problematic. There could be cases where a single complex item is encountered that was not clear at the engagement acceptance stage. The final paragraph in A9 states that the “presence of one characteristic exhibited by an entity does not necessarily exclude the use of the ISA for LCE for that entity”. However, the introductory sentence states “the ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics”. The use of professional judgment is important, but this may cause auditors confusion. The introduction could be clarified to capture the same sentiment as the first paragraph.

Malaysian Institute of Certified Public Accountants

Consequently, the definition of “Less Complex Entities” needs to be extremely comprehensive and robust to limit such uncertainties. Otherwise as explained, practitioners would rather continue to adopt the extant ISAs instead of taking the risk of reversing the whole LCE procedures to full-ISA procedures where one single complex item is identified at the middle of the audit process. Additionally, the IAASB may want to consider still allowing the use of this proposed ISA even if one new item of complexity is identified under certain prescribed conditions.

Given that there is no “flexibility” allowed in this proposed ISA, there are likely to be instances where new information that warrants the use of the extant ISAs appears in the midst of the execution of audit. In these circumstances, the change of standard from this proposed ISA for LCE to the extant ISAs will be required which will inadvertently result in an increase in the cost of compliance.

South African Institute of Chartered Accountants (2)

The impact of circumstances outside the control of the entity has not been factored into the standard. For example, the global COVID-19 pandemic created a lot of uncertainty and doubt about the going concern status of most entities. South Africa recently experienced riots that affected a lot of entities. As these situations are unexpected and are outside the control of the entity, the LCE standard needs to include considerations that address such situations. The complexity that these situations pose may require that the auditor jumps between the LCE standard and the ISAs in different periods.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2b) Burdensome or Hard to Implement\Interpretation by Others (e.g., Regulators)

3. Regulators and Audit Oversight Authorities

Irish Auditing and Accounting Supervisory Authority

It would also be a challenge for oversight bodies to assess and enforce whether the use of the standard is appropriate or not based on the current criteria.

4. National Auditing Standard Setters

American Institute of Certified Public Accountants

While we support the principle of the auditor applying professional judgment, we believe the shortcomings in the Authority Document will confound the appropriate exercise of professional judgment, inevitably resulting in

Challenges to the auditor’s determination by third parties

Canadian Auditing and Assurance Standards Board

Practitioners may be hesitant to use ISA for LCE. There are many consequences of concluding on the use of the standard incorrectly (e.g., inspection risk or transition to the ISAs mid-engagement). Practitioners may be reluctant to use the standard to avoid the risk of being challenged by practice inspectors on their application of professional judgment or having to transition to the ISAs mid-engagement. As a result, practitioners may be less willing to use the standard.

Difficult to regulate. Regulators have told us that it would be difficult to inspect whether the practitioner has reached the appropriate conclusion on the use of ISA for LCE due to the wide interpretation and significant professional judgment involved in the Authority.

7. Professional Accountancy and Other Professional Organizations

Korean Institute of Certified Public Accountants

Different stakeholders may make different judgments as to whether an entity is an LCE or not, which may become a source of conflict. For example, as to whether or not to use the ISA for LCE has impact on audit time, fees, and an entity's efforts to handle audit, the entity may challenge the auditor's determination as to whether the entity is an LCE or not. In addition, the regulator may disagree with the auditor on determination of LCE.

The auditor faces far more serious consequences if he or she determines a non-LCE as an LCE than the other way around. As a result, the auditor may avoid making decision even when necessary, and tends to choose not to use the ISA for LCE. This tendency may be encouraged by the requirement in paragraph A.9 of Explanatory Memorandum "If there is uncertainty about whether an audit is an audit of the financial statements of an LCE, the use of the [draft] ISA for LCE is not appropriate".

Malaysian Institute of Certified Public Accountants

In the event that the IAASB goes ahead to issue the LCE as a standard, strict parameters should be implemented as to which entities are applicable to use the proposed ISA for LCE so as to minimise disputes between audit firms, regulators, clients and even potential litigants.

There are concerns on the authority given to an engagement partner as circumstances may arise when the use of this proposed ISA for LCE is challenged by the jurisdiction/regulators/authorities. As the responsibility principally lies with the engagement partner to decide as to whether this proposed ISA for LCE can be used for an engagement, inevitably practitioners would choose the "safety" of the extant ISAs whenever there may be such uncertainty of this choice.

Polish Chamber of Statutory Auditors Warsaw (Regional Branch)

Disputes over the applicability of the standard.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2b) Burdensome or Hard to Implement\Hard to Use or Implement

4. National Auditing Standard Setters

Federación Argentina de Consejos Profesionales de Cs. Económicas

We consider that section A.8. (qualitative characteristics) of the draft standard has a high degree of subjectivity that can complicate the implementation and assign excessive responsibility in the evaluation.

Institute of Chartered Accountants of India

We agree with "Specific prohibitions" given in the Authority of the Standard. However, we have strong reservations regarding "Qualitative characteristics" due to following reasons:

- Qualitative characteristics are highly subjective in nature and require use of high level of professional judgment on part of auditors.

- It will require auditors to make detailed risk assessment of the entity before accepting the engagement in order to decide whether ISA for LCE can be used.
- It is putting all responsibilities on auditors to decide which standards is to be used for audit.

Malaysian Institute of Accountants

There is another issue that could be problematic. The IAASB is currently not proposing to allow any flexibility and requires the auditor to “check” that the application is still appropriate as the audit progresses. This may in practice be problematic, where, for example, a single complex item is encountered that was not clear at the engagement acceptance stage. This will also affect the adoption of the LCE standard in the market, as LCE practitioners would rather continue to adopt the full ISA instead of taking the risk of reversing the whole LCE procedures to full-ISA procedures where one single complex item is identified at the middle of the audit process. We suggest that a single matter alone should not trigger a move to the full ISAs. Instead, we would suggest for the IAASB to consider developing an alternative approach that would allow the auditor to supplement the LCE standard with a module especially designed to address that single matter on hand provided certain condition(s) are met.

7. Professional Accountancy and Other Professional Organizations

Polish Chamber of Statutory Auditors Warsaw (Regional Branch)

Disputes over the applicability of the standard.

Saudi organization for Chartered and Professional Accountants

As highlighted before, the excessive use of the “prohibitions” terminology may discourage auditors from using the standard because they could broadly find no major differences to the work they are anticipated to do in terms of the full ISAs’ requirements to achieve the reasonable assurance and offer the appropriate quality. They are eventually expected to use their judgment to determine the appropriateness of implementing the proposed standard to an entity.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2b) Burdensome or Hard to Implement\z) Other

7. Professional Accountancy and Other Professional Organizations

Chartered Accountants Australia and New Zealand and the Association of Chartered Certified Accountants

In our view, if the scope of the standard is too limited, it will discourage adoption by practitioners. From our outreach, the practitioners who see the most value in this standard are generally those who believe they will be able to audit all, or a large majority of, their clients under ISA for LCEs.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2c) Standard Used Inappropriately

3. Regulators and Audit Oversight Authorities

Independent Regulatory Board for Auditors (IRBA)

The unintended consequence of using the proposed standard when it should not be used would result in the auditor not obtaining sufficient appropriate audit evidence to support a reasonable assurance opinion and potentially expressing an inappropriate opinion. The Authority of the proposed standard thus needs to be sufficiently robust to avoid these eventualities.

4. National Auditing Standard Setters

American Institute of Certified Public Accountants

While we support the principle of the auditor applying professional judgment, we believe the shortcomings in the Authority Document will confound the appropriate exercise of professional judgment, inevitably resulting in:

Inappropriate application to audits of financial statements of entities to which the Exposure Draft is not intended to apply;

Canadian Auditing and Assurance Standards Board

Yes. The Authority is open to interpretation and significant judgment. As a result, the following unintended consequences could arise:

use of ED-ISA for LCE when inappropriate; and

5. Accountancy Firms

PriceWaterhouseCoopers

We believe there are two specific unintended consequences that could result from the proposed approach to drafting of the Authority section that the Board needs to reconsider:

As noted in our response to part (a), the potential to apply the standard on larger private entities may result in risks to audit quality if the work effort that would result from applying the standard is not deemed commensurate with the nature and circumstances of the entity and its operations.

7. Professional Accountancy and Other Professional Organizations

ASSIREVI

There could be an issue with the potential inconsistent application of the Authority in the long term that could prevent the use of ED-ISA for LCE or trigger its discontinuation depending on the entity's qualitative characteristics. We believe that, over time, the existence of auditors specialised in the audit of LCEs and, therefore, with less expertise with the ISAs, could imply that these auditors would not have all the knowledge necessary to appropriately evaluate the qualitative characteristics. This would increase the risk of the inappropriate application of ED-ISA for LCE.

Chamber of Financial Auditors of Romania

Our concerns also regard the implications of the possible errors in applying the ISA for LCE by an auditor when ISAs should, in fact, have been applicable. This will result in the new auditor facing challenges regarding comparability and the necessity to extend audit procedures in order to cover areas not taken into consideration by the previous auditor when using ISA for LCE. Also, we are concerned about the implications of transitions from LCE audits to ISA audits, especially considering the number of companies that are growing. Therefore, further guidance on the Authority of the new standard will result necessary.

CPA Ireland

We consider that careful consideration will be required at a jurisdictional level to determine the scope of the standard. It is at this point in the national approval process that it will be essential that due process is

afforded to ensure that there are no local unintended consequences, such as the application of the standard to a particular entity that would not be appropriate or for the reverse to happen.

Institute of Certified Public Accountants of Cyprus

Additionally, in the absence of clearly defined criteria/thresholds to establish what constitutes an LCE there is a likely risk that audit quality could be compromised if the audit effort, on the basis of the standard, is not commensurate to the true profile and characteristics of the relevant entity.

Pan-African Federation of Accountants (PAFA)

The unintended consequence of using the proposed standard when it should not be used, resulting in the auditor not obtaining sufficient appropriate audit evidence to support a reasonable assurance opinion and potentially expressing an inappropriate opinion, would be severe. Therefore, the Authority of the proposed Standard needs to be sufficiently robust to avoid these eventualities.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2e) User Perception (Authority Specific)

1. Monitoring Group

International Forum of Independent Audit Regulators (IFIAR)

The provisions contained in the exposure draft leave room for the auditor to evaluate whether the standard is applicable to an audit, and this could lead to situations where different auditors, firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities that exhibit similar characteristics. This may contribute to confusion for users of the financial statements and undermine the objective of achieving global consistency.

3. Regulators and Audit Oversight Authorities

Finance Professions Supervisory Centre Indonesia

Although the ED ISA for LCE sets out requirements that, taken together, would fulfil the overall objective of the auditor (i.e., to express an opinion based on the audit evidence obtained), users may not understand this when they see different auditor's reports, does it use the ISAs approach or ISA for LCE approach. The stakeholders (for example: banks, tax authority, etc) who reads these auditor's reports will not understand the difference why the auditor chooses to audit an entity with ISAs or ISA for LCE. The proposed standard could widen the expectation gap around levels of assurance but it potentially caused confusion in the marketplace.

Irish Auditing and Accounting Supervisory Authority

The scope of the ISA for LCE is subjective and likely to lead to inconsistent use of the standard. The provisions contained in the exposure draft leave room for the auditor to evaluate whether the standard is applicable to an audit, and this could lead to situations where different auditors, firms and/or jurisdictions may interpret the acceptability of using the ISA for LCE differently for entities that exhibit similar characteristics. This may contribute to confusion for users of financial statements and undermine the objective of achieving global consistency.

4. National Auditing Standard Setters

American Institute of Certified Public Accountants

If the concerns regarding the lack of a definition of an LCE or the Authority Document are not addressed, it is probable that there will be substantial confusion and uncertainty among users and other important stakeholders about when the Exposure Draft should be used and what it means when it is applied.

Reduced confidence in the value of an audit performed in accordance with the Exposure Draft as compared to an audit performed in accordance with the ISAs; and

Australian Auditing and Assurance Standards Board

There were also concerns that the high level of subjectivity included in the different qualitative characteristics which currently govern the use of the proposed standard may lead to inconsistent application in practice and unintentionally undermine the confidence users have on LCE audits.

5. Accounting Firms

KPMG IFRG Limited

Furthermore, if the auditor were to decide that it would be more appropriate to use the full-scope ISAs because of matters such as potentially complex going concern assessments during times of economic volatility, this could cause confusion for users of the financial statements who may not understand the underlying reasons for the transition, and may have a perception that the change in risk is greater than it really is. This could cause confusion in the marketplace, when the driver is not related to the entity specifically, as well as potentially placing the auditor in a difficult situation, e.g., if there were to be pressure from management not to use the full-scope ISAs to avoid creating an impression that complexity and risks relating to the entity are greater than they perhaps are.

5. Accounting Firms

PriceWaterhouseCoopers

Further, the level of subjectivity in the Authority will likely lead to inconsistency in the appropriate use of ISA for LCE versus the ISAs in similar fact patterns, which would be undesirable from an audit quality and comparability perspective (including potential confusion from users of the financial statements with regard to the level of audit work performed on audits of similar entities)

7. Professional Accountancy and Other Professional Organizations

Chamber of Financial Auditors of Romania

One unintended consequence might be that users of the audit report who are not familiar with the two sets of standards could raise suspicions regarding the amount of work carried out by the auditor using the ISA for LCE, as well as regarding the quality of the audit performed. Practitioners to this day face challenges in the market due to stakeholders' lack of understanding of the value of an audit and its benefits for the public interest and economic environment.

Confederation of Swedish Enterprise

Further, if audit firms apply different policies regarding the use of ISA for LCE in a specific jurisdiction this might also lead to confusion. Differences in the application of audit standards might be that difficult to understand for stakeholders. If such consequences are unintended or not can be debated.

Institute for the Accountancy Profession in Sweden (FAR)

For the qualitative characteristics the auditor is expected to use professional judgement. Most entities will probably be rather clear to assess whether they are LCE or not. However, there might be instances where two auditors come to different conclusions regarding the complexity assessment. In rare situations this might confuse clients and the regulators.

If firms or networks decide not to allow the use of the standard this might confuse stakeholders and impair the public interest's understanding of the standard.

Union of Chambers of Certified Public Accountants of Turkey (TURMOB)

IAASB need carefully communicate the authority, scope, assurance level, quality of ISA for LCE to manage expectations of various stakeholders considering public interest. This is crucial for avoiding new creation of expectation gaps regarding the standard as it comes in use.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2f) Opinion Shopping & Competition

3. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies

The lack of objective criteria included in the ISA for LCE to determine its suitable application may lead to possible bias by auditors in the qualitative analysis, in order to apply this standard and may even lead auditors to compete on whether or not an audit could be performed under the ISA for LCE, determining an inappropriate application of the standard and preventing auditors from changing to a full ISA audit if needed. The lack of indisputable criteria could also lead to some pressure by entities on the auditor to carry out an audit applying the ISA for LCE, with a perspective to reduce costs and audit quality.

Independent Regulatory Board for Auditors (IRBA)

In our view, a possible unintended consequence could be inappropriate competition among audit firms where, for example, one audit firm correctly concludes that the proposed standard is not applicable vs an audit firm that inappropriately concludes it is applicable. This would be due to different professional judgments applied in reaching a conclusion as to whether the proposed standard may be applied, based on the qualitative considerations where they are not specifically excluded by the proposed standard. Audit quality could be sacrificed if the work effort that would result from applying the proposed standard is not considered sufficient with reference to the nature and circumstances of the entity and its operations. Audit inspection findings are not limited to listed and PIE audits but to all segments of the audit market. Further, refer to our comments under General, and responses to questions 1(a) and 3(a).

Irish Auditing and Accounting Supervisory Authority

Further, the lack of objective criteria in the ISA for LCE to determine its suitable application may lead to possible bias by auditors in their qualitative analysis in order to apply this standard. It may even lead auditors to compete on whether or not an audit may be performed under the ISA for LCE, determining an inappropriate application of the standard and preventing auditors applying the full ISAs if needed. The lack of objective criteria could also lead to pressure by some entities on the auditor to apply the ISA for LCE with a view to reducing costs which may also reduce audit quality.

4. National Auditing Standard Setters

Indonesian Institute of Certified Public Accountants (IAPI)

A related risk arising from the judgement framework is whether this may encourage “inappropriate competition” i.e., entities actively seeking an audit firm that is willing to designate the entity as less-complex simply for purposes of being able to apply the ISA for LCE in order to reduce audit costs. That would clearly not be in the interests of achieving and maintaining audit quality.

New Zealand Auditing and Assurance Standards Board

However, the extent of judgement involved in the consideration of the QCs by the firm or at the engagement level in the scoping of the standard might create inconsistency in practice whereby different auditors may arrive at different conclusions as to whether the same entity could qualify as an LCE. This could result in ‘opinion shopping’ by clients, especially if there is a misperception that LCE audits may cost less but achieve the same level of assurance, which is a fundamental perception issue. This perception risk should be addressed especially in light of the recent revision to the fee-related provisions of the IESBA Code of Ethics (the Code), that highlights that fee considerations also include factors such as cost of resources, duration and timing of audit as well as quality of management’s record keeping and processes for financial statements preparation (Paragraph 410.23 A1 of the Code).

5. Accounting Firms

Ernst & Young Global Limited

There is a risk that issuing a separate standard will result in the creation of two tiers of entities under the International Standards on Auditing – complex entities and less complex entities. We believe that the

creation of two tiers of entities will create expectations from audited entities regarding their classification of an entity as complex or less complex.

We also believe that an inevitable consequence will be the creation of two tiers of entities under the International Standards on Auditing – complex entities and less complex entities. We believe that the creation of two tiers of entities will create expectations from audited entities regarding their classification of an entity as complex or less complex. Issues for auditors could arise when a client wants to be classified as a LCE so the audit can be conducted under the ED-ISA for LCE. For example, there could be a scenario where an entity may pressure competing auditors to make decisions about the complexity of the entity prior to being engaged to set expectations about lower fees (i.e., entities may believe that fees should be lower because the auditor has a less complex audit to perform). This would then in turn create undue pressure on auditors to maintain their original complexity assessment after accepting the audit and understanding the business model in greater depth.

7. Professional Accountancy and Other Professional Organizations

Korean Institute of Certified Public Accountants

Different stakeholders may make different judgments as to whether an entity is an LCE or not, which may become a source of conflict. For example, as to whether or not to use the ISA for LCE has impact on audit time, fees, and an entity's efforts to handle audit, the entity may challenge the auditor's determination as to whether the entity is an LCE or not. In addition, the regulator may disagree with the auditor on determination of LCE.

South African Institute of Chartered Accountants (2)

Inappropriate competition among firms may arise due to their different judgements used in reaching a conclusion on whether the LCE standard may be applied to the audits of their entities based on the qualitative considerations where they are not specifically excluded by the LCE Standard.

Section 4B – Authority of the Standard\Question 3 - Views on the Authority of ED-ISA for LCE \Question 3(b) - Are there unintended consequences that the IAASB has not yet considered\2) Yes with Comments\2z) Other Comments

5. Accounting Firms

KPMG IFRG Limited

In describing pervasive risks, these are linked to entity characteristics, such as the entity's business model, or the jurisdictions in which it operates. However, pervasive risks may also be affected by matters external to the entity and therefore outside of the entity's control, e.g., going concern risk may be driven more by the economic environment in which the entity operates, even though this significantly interacts with entity-specific characteristics in addition. However, as drafted, the authority of the standard would not necessarily steer an auditor to use the full-scope ISAs in the event that an LCE faced complexity with respect to the going concern assessment. (Refer to our comments in response to Question 3c).

6. Public Sector Organizations

Office of the Auditor General of Alberta

As noted in Section 1 of the Exposure Draft, "It is estimated that more than 90% of entities across the world are small and medium-sized entities..." Given the majority of entities are either small or medium-sized entities, ED-ISA for LCE has the potential to be the common standard globally and the ISAs for More Complex Entities becomes the standard for complex and listed entities, the remaining 10% of entities. Another possible consequence is that users of ISA will use the guidance within ISA for LCE in their interpretation of the ISAs. For example, ED-ISA for LCE 6.3.14 includes an example where "the auditor may determine that there are no identified controls other than the entity's controls over journal entries" for which "it is necessary for the auditor to evaluate the design of controls and determine that they have been implemented." Note - see response to Question 9 for further comments

7. Professional Accountancy and Other Professional Organizations

Chamber of Auditors of the Republic of Azerbaijan

The scope as presented is theoretically implementable.

(b) However, there may be unintended consequences that the IAASB has not yet considered.

CPA Ireland

We consider that careful consideration will be required at a jurisdictional level to determine the scope of the standard. It is at this point in the national approval process that it will be essential that due process is afforded to ensure that there are no local unintended consequences, such as the application of the standard to a particular entity that would not be appropriate or for the reverse to happen.

Institute of Chartered Accountants in England and Wales

We think unlikely that IAASB has left many stones unturned, but we urge it to engage with audit regulators individually and collectively to address their concerns and to emphasise IAASB's belief in the public interest in this standard.

Audit regulators in developed jurisdictions in which there are high audit exemption limits, or no audit requirements at all outside the listed sector, may ignore this standard. If they do, they risk seeing it take on a life of its own in a commercial context, outside existing regulatory and standard-setting structures.

We understand the reason for the exclusion of all listed entities, some of which are quite simple, but care needs to be taken with the messaging to ensure that stakeholders understand that this standard provides the same level of assurance as the extant ISAs.

IAASB should also engage closely with Supreme Audit Institutions to ensure appropriate and consistent adoption of the standard in the public sector.

Institute of Chartered Accountants of Scotland

An unintended consequence that might result from the exclusion of all groups is that the standard may not be applicable to as wide a range of audits of LCEs as it should be. That, therefore, might mean that the finalised standard will not be adopted by those jurisdictions which have either implemented their own standard or are on the verge of doing so. Additionally, even where audit firms are allowed to adopt the standard, if they have a number of group audits which are less complex in nature, this blanket prohibition might mean that they opt to continue with the full suite of ISAs for all of their audits.

Malta Institute of Accountants

As already mentioned above, some unintended consequences which could arise include:

More confusion and hence more ambiguity, due to lack of detailed examples and clarity as to how the ISA for LCE is to be adopted and how it will impact procedures when compared to procedures under ISAs.

There is concern that if trying to keep aligned with the ISAs, changing the wording of the requirements introduces ambiguity about whether the intent is the same or not. In the current environment, opening the door to different interpretations is not in the public interest and increases the expectation gap.

8. Academics

Accounting and Finance Association of Australia and New Zealand

We believe that the Authority may lead to confusion as to the applicability of the standard in that it will likely contribute to a disconnect between what is perceived to be a less complex entity and entities scoped into the standard. We recommend that the IAASB consider placing less emphasis on global prohibitions and more emphasis on qualitative characteristics and jurisdictional discretion.

We are concerned that the authority may be such that there is a disconnect between the entities for whom the standard is written (i.e., less complex entities) and the entities for whom the authority allows its use. With reference to the IASB standard for small to medium enterprises, research highlights potential consequences when there is a lack of correspondence between the entities for whom the standard applies (i.e., small to medium enterprises) and perceptions of the entities who can and cannot apply the standard (Perera and Chand 2015). To the extent that the authority scopes out entities that may otherwise be perceived to be less complex in the particular jurisdiction, this may lead to challenges in the implementation and use of the standard.

We recommend that the IAASB, in reflecting on the authority, allow for a closer alignment between what is understood to be a less complex entity and those entities scoped into the standard by focusing more on qualitative characteristics and jurisdictional discretion rather than global prohibitions.