

Supplement 2-11 to Agenda Item 6

Audits of Less Complex Entities – ED-ISA for LCE – Q4 (b) - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE? If not, why and what changes (clarifications, additions or other amendments) need to be made?

Please distinguish your response between the: Qualitative characteristics

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\1) Yes

4. National Auditing Standard Setters

Austrian Chamber of Tax Advisors and Public Accountants (KSW)

Yes, we agree.

Compagnie Nationale des Commissaires aux Comptes and Conseil Supérieur de l'Ordre des Experts-Comptables

We agree with the proposed limitations relating to the use of ED-ISA for LCE, both in terms of specific prohibitions and qualitative characteristics.

5. Accounting Firms

Crowe Global

We agree with the proposed limitations, with the exception to those that relate to the application of the standard for the audit of group financial statements.

Crowe Macro Brazil

Fully agreed.

MHA Monahans

Apart from (d) in specific prohibitions, we agree with the proposed limitations.

Sayer Vincent LLP

Agree with this and understand the limitations in being able to provide specific examples.

6. Public Sector Organizations

Audit Scotland

Yes.

Auditor-General of New Zealand

The qualitative characteristics provide an adequate framework that can be used by auditors and their firms to develop a policy that regulates the application of the proposed standard to the entities, and classes of entity, that the firm audits.

Government Accountability Office (USA)

The proposed limitations identified in the Authority are sufficient. The inclusion of specific prohibitions and qualitative characteristics provide sufficient depth for considering the types and nature of entities that are not within scope of an LCE.

7. Professional Accountancy and Other Professional Organizations

Chamber of Auditors of the Republic of Azerbaijan

We basically agree with the proposed limitations on application of ED-ISA for LCE.

Chamber of Financial Auditors of Romania

Our opinion is that the specific prohibitions as well as qualitative limitative characteristics are deemed necessary and we agree with those proposed in the standard.

Chartered Governance and Accountancy Institute in Zimbabwe

agree with the proposed limitations relating to the use of ED-ISA for LCE.

CPA Australia

We support the specific prohibitions and qualitative characteristics limiting the use of the standard. We reiterate that a post-implementation review can consider whether changes are needed based on the experiences of implementation.

Federation of Accounting Professions of Thailand

Yes.

Indonesian Committee on Public Accountant Profession (KPAP)

We agree with the proposed limitations relating to the use of ED-ISA for LCE.

Institute of Certified Public Accountants of Rwanda

We agree on both qualitative and specific prohibitions but on the latter, we have sought more clarification to be made on section 5: Group audits.

Instituto dos Auditores Independentes do Brasil

Yes. We agree with the limitations including listed entities and group audits.

Instituto Mexicano de Contadores Públicos (IMCP)

Yes, we agree except for the exclusion of Group audits, which is dealt with in Section 5, questions 22 to 26 of this document.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. Accounting Estimates

3. Regulators and Audit Oversight Authorities

Independent Regulatory Board for Auditors (IRBA)

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 such an 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.

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Clarify the Authority to address common complexities more clearly. The Authority should clarify what “less complex” means. Most entities have accounting estimates. Whether such estimates are subject to a higher degree of estimation uncertainty is subjective. We believe that there are some complexities that are common in LCEs, and their presence should not make the standard inappropriate to use.

They provided the following specific examples:

Characteristic of “The entity’s accounting estimates are subject to a higher degree of estimation uncertainty, or the measurement basis required complex methods that may involve multiple sources of historical and forward-looking data or assumptions, with multiple interrelationships between them”

The field-testing showed that it was common for an LCE to have some elements of complexity in their accounting estimates that may be deemed to have a higher degree of estimation uncertainty. The field-testers were unclear whether, and if so, how many, complexities in the accounting estimates would make the standard inappropriate for use. They were also unclear whether a one-time accounting estimate that includes an element of complexity would make the standard inappropriate for use.

Examples of accounting estimates where it was unclear whether they would make the standard inappropriate for use include:

- indicators of impairment;
- goodwill, intangibles or accounting for business combinations;
- foreign currency transactions;
- inventory provision; and
- valuation of livestock (e.g., cattle) or fruit orchards in the farming/agriculture industry that is deemed a complex estimate due to the data and computations used.

We suggest the following solutions to address these concerns:

What stakeholders told us

For 9 of the audit files field-tested, practitioners told us that the assessment of the qualitative characteristics is open to interpretation and requires significant professional judgment.

Hong Kong Institute of Certified Public Accountants

Applicability of ED-ISA for LCE to entities with accounting estimates

As currently drafted, ED-ISA for LCE is inappropriate if the entity’s accounting estimates are subject to a higher degree of estimation uncertainty or the measurement basis requiring complex methods that may involve multiple sources of historical and forward-looking data or assumptions, with multiple interrelationships between them. (paragraph A.9. of ED-ISA for LCE)

The IAASB provides additional information on the application of the ED in the proposed Authority Supplemental Guide. It includes an example that the proposed standard is inappropriate in the case of fair value accounting estimates that use unobservable inputs, i.e. Level 3 inputs under IFRS 13 Fair Value Measurement, to measure fair value of an asset or liability.

In Hong Kong, it is common for a non-regulated private entity, without substantial businesses and/or operations, solely to hold an investment property (IP) accounted for using fair value with Level 3 inputs. The prohibition and example set out above would exclude an entity holding an IP from the scope of ED-ISA for LCE, although it would otherwise qualify as an LCE under the proposed standard.

We would recommend the IAASB to re-consider whether in the specific circumstance that entities holding IPs with fair value accounting estimates using Level 3 inputs would automatically be ruled out from applying ED-ISA for LCE in their audits. Particularly, we suggest the IAASB to remove explicit reference to the fair value hierarchy in IFRS 13 when describing the restriction concerning auditing accounting estimates, recognizing the following:

While an IP valuation would typically require Level 3 inputs, property markets in jurisdictions such as Hong Kong are active and transparent with readily available historical and forward-looking data or assumptions. This is evidenced by the instant and free-of-charge property valuation services for major residential properties offered by a number of valuation companies and banks in Hong Kong to assist property buyers to assess the property values.

Although significant judgement (i.e. unobservable input) is required to determine each IP valuation to account for differences in location, building condition etc., most IP valuations in Hong Kong are performed by professional valuers using recognized valuation framework and techniques. Despite the use of Level 3 inputs, market transparency and the use of professionals to perform the valuation has greatly reduced the uncertainty in an IP valuation.

Specifying prohibition with reference to the fair value hierarchy in IFRS 13 would be too rigid, prescriptive and moving away from the “principle-based” approach intended for ED-ISA for LCE.

In addition to the above, we also propose enhancing the requirements and materials on auditing accounting estimates in ED-ISA for LCE to expand its scope to deal with accounting estimates involving circumstances such as those relating to the IP valuation

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

In addition, the seventh bullet in paragraph A.9 can be clarified by referring to the need to apply an expected loss model or to value complex financial instruments for which there are no robust market prices.

Malaysian Institute of Accountants

Furthermore, we believe the issue on accounting estimates can be clarified or examples should be added specifically, as it relates to fair value measurements where level 3 inputs are used. We believe there could be situations whereby an LCE holds investments where level 3 inputs are used to measure fair value, but otherwise meet all other qualitative characteristics to qualify as an LCE for purposes of this standard. In this regard we refer to our suggestion in Q3(b) above regarding a supplementary module that can be made available to deal with a one-off complexity.

5. Accounting Firms

BDO International

We debated whether the need for an auditor’s expert on the engagement should be a qualitative consideration when determining if an entity can use the LCE standard. However, if the IAASB agrees with our suggestion of allowing estimates with high estimation uncertainty in the proposed LCE standard, then we would need to allow the use of an auditor’s expert. Therefore, we would not want this added as an additional qualitative characteristic, assuming estimates are added to the scope of the proposed standard.

The inclusion of estimates with high estimation uncertainty in the qualitative characteristics that preclude use of the LCE standard causes significant concern. Even very simple entities will have estimates under most applicable financial reporting frameworks, and many of those estimates will have high estimation uncertainty. We believe that such entities, assuming other qualitative characteristics are met, should be able to use the LCE standard. If such estimates are not removed from the qualitative characteristics, engagement teams may try to justify that there is not high estimation uncertainty simply to use the LCE standard. Alternatively, practitioners may decide that it is easier not to adopt the proposed LCE standard at all, perhaps adopting a local LCE standard instead, which does not help the IAASB achieve its objective of a global LCE standard.

Ernst & Young Global Limited

However, it is our view that excluding specific procedures in relation to complex accounting estimates will make the ED-ISA for LCE not applicable to many LCEs. We understand that certain specific procedures concerning the use of complex modelling and detailed requirements addressing situations where there is higher estimation uncertainty have not been included in the ED-ISA for LCE as the IAASB has indicated that they are not expected to be relevant for the types of accounting estimates in an audit of a typical LCE. However, it is our view that the complexity of the underlying accounting estimate should be considered when considering the Authority of the ED-ISA for LCE. For example, a common situation for an LCE may be the impairment of their non-current assets that may use more complex modeling. However, because of the potential complexity in determining this estimate, there may be situation where auditors would not be able to use the ED-ISA for LCE. As a result, we suggest that the IAASB revisit this decision to exclude certain specific requirements from the ED-ISA for LCE related to accounting estimates. We believe that the presence of a complex characteristics should be determined based on judgment by the auditor about whether it is still appropriate to perform the audit under the ED-ISA for LCE. The auditor would need to determine if the complex matter or circumstance identified is not in the spirit of what the standard intended to be allowed as an accounting estimate.

However, if the IAASB was to adopt our suggestion to narrow down the criteria in the Authority to make the ED-ISA for LCE applicable to only entities at the lowest level of complexity (i.e., refine the authority of use) then this prohibition on complex estimates would be more understandable.

ETY sas

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.

Grant Thornton International Limited

As noted in our response to question 3, we are concerned with the inclusion of the qualitative characteristic of accounting estimates. Whilst the concept of prohibiting the use of the Proposed Standard for entities that have accounting estimates with high estimation uncertainty is a reasonable concept, we are of the view that better guard rails are needed around how and when estimates meet this criterion. Even with the inclusion of the table in the Supplementary Guidance, we believe that this criterion may give rise to inappropriate application of ED-ISA for LCE and can only result in its inconsistent use; both on a period-to-period basis and a firm-to-firm basis.

MNP LLP

Accounting estimates

Paragraph A.9 includes the characteristic of “...accounting estimates [that] are subject to a higher degree of estimation uncertainty or the measurement basis requires complex methods...”. We believe there are many entities that should be considered less complex, however contain one or two accounting estimates with a

higher degree of estimation uncertainty. For example, there may be entities in the agriculture industries that have simple, less-complex operations however they have livestock (e.g., cattle) or fruit orchards that are treated like a complex estimate in audit due to the data and computations used. As well, if any intangible rights or goodwill are determined to be complex estimates, this will exclude a significant number of entities that otherwise would have been deemed to be less complex.

We expect that this qualitative characteristic will come up for many LCEs that undergo business combinations given there are typically more complicated estimates involved. This results in one year where the entity is deemed complex followed by the entity being deemed less complex in subsequent years. This will have further impacts on the audit opinion and the users' perception of the audit report when practitioners are required to report using the LCE standard and then having to change to the full suite of ISAs due to the business combination (i.e., audit report's prepared in accordance with different auditing standards). We believe that a practitioner should be able to use the ISA for LCE standard, consistently year-to-year, in scenarios where there are a limited number of estimates.

Price Bailey LLP

As noted above the qualitative characteristics are not clear enough and therefore could lead to misunderstanding, inconsistencies and challenge from regulators.

Key areas as noted above is around the accounting estimates.

In A9, at the 7th bullet point it refers to "complex methods" with accounting estimates. There could be a number of different interpretations of the types of accounting estimates which would meet that definition, as different firms / audit engagement partners may classify "complex methods" differently. Something that may be seen as complex to one audit partner may seem less complex to someone else who specialises in a particular area.

There can also be accounting estimates which have a higher degree of uncertainty however we do not believe that in its self should mean that this draft standard couldn't be applied. Although there is the supplementary guidance that has been issued you need more specific examples, for example, investment property valuation, or share option schemes, or defined benefit pension schemes. Some very simple companies may have these and different auditors which have different views as to whether these are complex or not.

The authority is not sufficiently prescriptive in regard to the reference to complex accounting estimates. Without clarity in this area we are concerned that there will be different interpretations, including between firms and regulators.

PriceWaterhouseCoopers

The entity's accounting estimates are subject to a higher degree of estimation uncertainty or the measurement basis requires complex methods... - Implementation of ISA 540 (Revised) has shown that this is an area where there are often significant interpretation differences as to both what comprises an accounting estimate and when an estimate is deemed to be subject to complexity. Clearer direction on this characteristic is more challenging but is perhaps the area that is driving most concern amongst stakeholders as to its interpretation. More examples of estimates, or methods, that are deemed less complex would likely help drive consistency in judgements made by auditors for similar fact patterns.

RSM International

Excluding an entity from ED-ISA for LCE on the basis of a single accounting estimate with higher complexity seems contradictory to the statement in paragraph A9 that "Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances". We consider that more flexibility is required in this area and that accounting estimates with higher complexity do not necessarily lead to the conclusion that the entity as a whole is complex.

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.

With respect to the more specific aspects, in our view, paragraph A.9 of the Authority (referring to the qualitative characteristic represented by the high degree of uncertainty and complexity of accounting estimates and the subsequent considerations about whether the presence of just one qualitative characteristic excludes the entity from the scope of the proposed standard) is not consistent with paragraph 27 of the Explanatory Memorandum.

This paragraph seems to imply that the proposed standard cannot be used "tout court" when the entity has a complex accounting estimate, as the rules established for this by ISA 540 have not been included in the standard and cannot be used to supplement it. Conversely, paragraph A.9 states that the presence of a complex accounting estimate is just one possible characteristic of "complexity" which does not per se exclude the entity from the scope of the proposed standard as the auditor should evaluate all the entity's qualitative characteristics, i.e., both those set out in the standard as well as others which may be material. The Authority Supplemental Guide (paragraphs 27 and 28) seems to agree with this approach. This Guide states that if an entity's financial statements include a caption subject to a complex accounting estimate (and, hence, one of those characteristics with a red "X"), this implies it has a qualitative characteristic not usually associated with an LCE. However, if the entity does not have other qualitative characteristics, it could meet the definition of an LCE and, therefore, the proposed ISA for LCE could be applied. Moreover, if the rules to be applied to audit the complex accounting estimates are not included in the proposed ISA for LCE and this proposed standard (due to its rigidity given the decision to make it a standalone standard, separate to the ISAs) cannot be supplemented with the requirements of ISA 540, it would be logical to conclude that the proposed standard cannot be applied when there are complex accounting estimates. To sum up, in our view, should the impossibility of supplementing the standard, as it currently stands, with other rules in the ISAs (e.g., ISA 540) be confirmed, the qualitative characteristic of complex accounting estimates should be treated separately and not as one of the characteristics set out in paragraph A.9 of the Authority and the table in paragraph 28 of the Authority Supplemental Guide.

The same considerations apply with respect to the use of a service organisation by an entity and the auditor's need to rely on reports on the operating effectiveness of the controls from the entity providing the services (e.g., "Type 1" and "Type 2" reports) and the rules of ISA 402 on their utilisation.

Association of Practising Accountants

In A9, at the 7th bullet point it refers to "complex methods" with accounting estimates. There could be a number of different interpretations of the types of accounting estimates which would meet that definition, as different firms / audit engagement partners may classify "complex methods" differently. Something that may be seen as complex to one audit partner may seem less complex to someone who specialises in a particular area.

There can also be accounting estimates which have a higher degree of uncertainty, however we do not believe that in itself should mean that this draft standard could not be applied. Although there is the supplementary guidance that has been issued there would be real merit in more specific examples, for instance on investment property valuation, or share option schemes, defined benefit pension schemes - some very simple companies may have these.

Chamber of Auditors of the Czech Republic

For estimates, we believe that it should be allowed to use ISA for LCE even if one or few complex estimates are present. In such case, the auditor shall be required to use ISA 540R (or other set of requirements) in addition to ISA for LCE. Similar solution shall also be available in the area of ownership and organisational structure and related party transactions.

Confederation of Swedish Enterprise

We believe that an alternative is to assess the applicable accounting standards for the entity instead of focusing on the accounting of a specific item. This means that local GAAP might have an impact on the

assessment of complexity. If the entity e.g. applies an accounting standard specially designed for SMEs, this could be an indication that the accounting is less complex.

We appreciate the examples in Draft Supplemental Guidance, but we think that there is a lack of a holistic view. In the examples, fair value accounting using Level 1 inputs passes as non-complex while fair value accounting using Level 3 inputs is deemed to be complex. Examples relating to a specific asset or a liability are of limited help when assessing the accounting policies of an entity. Should fair value accounting of a portfolio of financial instruments using Level 3 inputs lead to a classification of the accounting as complex if all other assets and liabilities are valued at historical cost in an entity? And should that have an impact on which auditing standard that should be applied?

We have some comments on the entity's accounting estimates. According to A.9. in the draft standard, that the entity's accounting estimates are subject to a higher degree of estimation uncertainty or that the measurement basis requires complex methods that way involve multiple sources of historical and forward-looking data or assumptions, with multiple relationships between them, is an indication that it is inappropriate to apply the ISA for LCE. In the Draft Supplemental Guidance a number of examples of accounting complexity is described.

We believe that starting point, i.e. estimation uncertainty, needs to be put into a perspective. There are very few assets that have reliable and observable market prices. Most assets and liabilities in a balance sheet are measured using a measurement technique, in accordance with the applicable accounting standard for the entity. This means that in most cases there will be some degree of measurement uncertainty present. Uncertainties will be resolved when the asset is sold or consumed or the liability is extinguished. We therefore think that it is somewhat difficult to assess "when there is a higher degree of estimation uncertainty or that the measurement basis requires complex methods that way involve multiple sources of historical and forward-looking data or assumptions". None of these features are defined in the draft standard and in order to assess when such a complexity is present, some type of "baseline" needs to be established.

Institute of Chartered Accountants in England and Wales

A9: 7th bullet refers to 'complex methods' with accounting estimates. The perceived complexity of methods depends on the skills and experience of the firm and engagement partner. Accounting estimates with a higher degree of estimation uncertainty should not themselves preclude application of the standard.

However, IAASB's guidance relating to accounting estimates, in relation to the level of complexity and the extent of uncertainty, needs work and we note in our answer to Question 3, above, our belief that high estimation uncertainty should not preclude the use of this standard.

Institute of Chartered Accountants of Ghana

The Entity's Accounting Estimates

The entity's accounting estimates are subject to a higher degree of estimation uncertainty

We are not sure why complex Revenue Recognition would not be a part of qualitative complex characteristics. Other than that, we do not have any additions or subtractions to these qualitative restrictions on the usage of the draft LCE.

International Federation of Accountants' Small and Medium Practices Advisory Groups

A.9 that states the following:

"The entity's accounting estimates are subject to a higher degree of estimation uncertainty or the measurement basis requires complex methods that may involve multiple sources of historical and forward-looking data or assumptions, with multiple interrelationships between them".

We believe this criterion should be clarified or examples should be added. Specifically, as it relates to fair value measurements where level 3 inputs are used. We believe there could be situations whereby an LCE holds investments where level 3 inputs are used to measure fair value, but otherwise meet all other qualitative characteristics to qualify as an LCE for purposes of the standard.

Additional examples of estimates that we believe could be fairly simplistic in many cases but might preclude use by entities otherwise considered to be LCEs as currently drafted include indicators of impairment, percentage of completion accounting, stock-based compensation, goodwill, foreign currency transactions, and inventory obsolescence provisions. Again, we believe that professional judgment should be applied in

such cases and the auditor could consult implementation guidance or other practice aids in limited cases, similar to how auditors currently apply judgment when determining whether the ISAs are the appropriate standards to be used in certain circumstances.

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

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.

Pan-African Federation of Accountants (PAFA)

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.

9. Individuals and Others

Vera Massarygina

Accounting estimates and limitations relating to the use of the standard should be analyzed more thoroughly as all necessary audit procedures for some accounting estimates may be fulfilled under audit of LCE.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. Business activities, business model and industry

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Characteristic of “Business activities, business model and industry”

Stakeholders noted situations where, while this circumstance may add complexity to the audit, the entity may still be less complex. For example, entering a new market could be a routine activity for a growth enterprise, or shifting from development to operations could be routine for start-up entities. It is unclear how this characteristic impacts the ability of the auditor to obtain sufficient appropriate audit evidence.

5. Accounting Firms

Grant Thornton International Limited

The table presented in paragraph 28 of the Supplementary Guidance for the Authority of the [Draft] Standard (the Supplementary Guidance), whilst a helpful aid to understand what constitutes qualitative characteristics, may be interpreted as a bright line as to when the standard can or cannot be applied. This may have the consequence of ED-ISA for LCE being excluded from use when its application to the audit of an entity may be appropriate. For example, in the Business Activities, Business Model or Industry section of the table, entities that are ‘start-ups’ are by default considered inappropriate to be audited under ED-ISA for LCE; however, not all start-up entities are complex in nature.

PriceWaterhouseCoopers

The entity's business activities, business model or the industry in which the entity operates results in pervasive risks that increase the complexity of the audit - This represents a highly judgemental determination that will be influenced by personal experiences of financial statement preparers and auditors with regard to perceptions of risk and complexity. We believe directly describing attributes of an entity's operations that are considered to be less complex is easier to visualise.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. Complex Transactions

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Characteristic of “Transactions are complex or the information system and related processes relevant to the entity's financial statements are complex such that data collection and processing involves complex accounting or calculations”

It can be common for LCEs to use information systems and related processes that may exhibit complexities, such as an online sales model. As the technology environment evolves, complexities in the information system and related processes of an LCE may become increasingly more common. This qualitative characteristic should be able to stand the test of time.

Our field-testers noted that it is unclear whether an entity that processes transactions online, for example, would be considered to have a complex information system and related processes. They noted that ISA 315 (Revised 2019), Appendix 5, provides characteristics of IT environments that may be less complex. They thought that including such characteristics in ISA for LCE would help improve clarity and interpretation of this qualitative characteristic.

We also heard suggestions that this characteristic covers two points:
transactions; and
information system and related processes.

Our field-testers noted examples where transactions are not complex, but the information system is complex (i.e., online transaction processing). They thought that the two points are independent of each other.

5. Accounting Firms

PriceWaterhouseCoopers

Transactions are complex or the information system and related processes relevant to the entity's financial statements are complex.... - Defining characteristics of complexity which themselves refer to complexity does not support auditors in understanding what may be deemed a complex transaction or a complex information system. Many information systems in today's business environment would likely be deemed complex to some degree. Again, we believe describing what types of information system or IT packages would be considered less complex helps remove much of the subjectivity and reduces the risk of inconsistent judgements being drawn by different auditors for similar fact patterns.

The entity's IT environment or IT systems are complex... - As per previous bullet.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. Development Stage or Emerging Economy

4. National Auditing Standard Setters

Hong Kong Institute of Certified Public Accountants

Paragraph A.9. of the ED includes an example that the proposed standard is inappropriate when an entity operates in new or emerging markets, or entities in the development stage because the resulting pervasive risks increase the complexity of the audit.

We consider the above examples are too restrictive and might result in an unintended consequence of excluding an otherwise simple entity from the proposed standard. For example, a start-up entity engaging in a straightforward, traditional business might be an LCE within the scope of the proposed standard. We believe the complexity of an entity does not necessarily relate to its stage of development.

Malaysian Institute of Accountants

In addition, we believe the characteristic in A.9 regarding the standard being inappropriate for entities in new and emerging markets, or entities in the development stage, is too restrictive in nature. There are many entities that happen to be in the development stage, but otherwise would qualify to use the standard. We believe that no matter what stage an entity is in, if it meets all of the other characteristics of an LCE, it should not be prohibited from using the standard.

New Zealand Auditing and Assurance Standards Board

Entities in the start-up stage indicates that the entity is complex. However, we not consider that start-ups are necessarily complex. At the initial stage they may just incur expenses and nothing else, and therefore may be less complex.

5. Accounting Firms

BDO International

With regards to paragraph A.9, an extract of the first bullet point reads: "... such as when the entity operates in new or emerging markets, ...". We believe that clarity is needed on this sentence because it appears that auditors of entities operating in emerging markets are automatically scoped out of the ISA for LCE.

MNP LLP

New/emerging markets and development stage companies

Paragraph A.9 also presumes that entities operating in new or emerging markets or entities in the development stage increase the complexity of the audit. Many development or exploration stage entities in a number of industries are less complex, from extractive industries through to biotech industries. We believe this language should be softened (e.g., "may increase the complexity of the audit") or removed to prevent truly less-complex entities from being scoped out of the ISA for LCE standard.

7. Professional Accountancy and Other Professional Organizations

Finnish Association of Authorised Public Accountants

We mainly agree with the qualitative characteristics, but we think that the examples given in A.9. can be too restrictive, especially if they are interpreted strictly without reading the Authority Supplemental Guide. For example, mentioning entities "in the developing stage" is too restrictive. Many SMEs start from scratch and therefore are in their first years in the development stage, but in all other respects they are less complex.

Institute of Certified Public Accountants of Uganda

We wish to point out that entities operating in a new or emerging markets should not be scoped out of the ISA for LCEs (see paragraph A.9) merely for that fact. Many entities operating in new or emerging markets are in fact simple in business operation and nature of activity. We recommend that the language in paragraph A.9 should be amended to prevent such less-complex entities from being scoped out of the ISA for LCEs.

Institute of Chartered Accountants of Pakistan

In addition to our response in question 3(a) above, we believe that the qualitative characteristic given in paragraph A.9 of the Exposure Draft regarding the proposed standard being inappropriate for entities in new and emerging markets, or entities in the development stage, is too restrictive in nature. The relevant paragraph is reproduced below for reference:

"...The entity's business activities, business model or the industry in which the entity operates results in pervasive risks that increase the complexity of the audit, such as when the entity operates in new or emerging markets, or entities in the development stage."

We understand that there are many entities that are either in new or emerging markets or in the development stage, but otherwise would qualify for using the standard. We believe that irrespective of the development stage and maturity of the entity, if it meets all of the other characteristics of a less complex entity, it should not be prohibited from the applicability of the standard.

International Federation of Accountants' Small and Medium Practices Advisory Groups

Further, we believe the characteristic in A.9 regarding the standard being inappropriate for entities in new and emerging markets, or entities in the development stage, is too restrictive in nature. There are many entities that happen to be in the development stage, but otherwise would qualify for using the standard. We believe that no matter what stage and entity is in, if it meets all of the other characteristics of a LCE, it should not be prohibited from using the standard. In other words, if the IAASB believes there are certain characteristics within an entity's start-up stage that would be so complex that the standard would not be applicable, those characteristics should be mentioned in the standard rather than referring so broadly to a certain stage in an entity's development.

Nordic Federation of Public Accountants

We believe the specific examples used to explain the characteristics in the first bullet in A.9., i.e. that the standard would be inappropriate to use on audits of entities in new and emerging markets, or entities in the development stage, are too restrictive. For example, one could quite easily argue that many (small and medium sized) entities are in the development stage, even though they in all other matters qualify for the use of the standard. Therefore, we encourage the IAASB to reconsider the impact keeping these examples would have on the use of the standard.

9. Individuals and Others

Vera Massarygina

some qualitative characteristics seem strange: for example – why companies in the start-up or development stage of its life cycle could not be treated as LCE?

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. IT Environment

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Characteristic of “Transactions are complex or the information system and related processes relevant to the entity’s financial statements are complex such that data collection and processing involves complex accounting or calculations”

It can be common for LCEs to use information systems and related processes that may exhibit complexities, such as an online sales model. As the technology environment evolves, complexities in the information system and related processes of an LCE may become increasingly more common. This qualitative characteristic should be able to stand the test of time.

Our field-testers noted that it is unclear whether an entity that processes transactions online, for example, would be considered to have a complex information system and related processes. They noted that ISA 315 (Revised 2019), Appendix 5, provides characteristics of IT environments that may be less complex. They thought that including such characteristics in ISA for LCE would help improve clarity and interpretation of this qualitative characteristic.

We also heard suggestions that this characteristic covers two points:
transactions; and

information system and related processes.

Our field-testers noted examples where transactions are not complex, but the information system is complex (i.e., online transaction processing). They thought that the two points are independent of each other.

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

We believe that the sixth bullet in paragraph A.9 can be clarified by referring to the far-right column of the table in Appendix 6 of ISA 315 (Revised 2019) in relation to large or complex IT applications, which should preclude the use of the LCE standard. We do not believe that referring to the ISAs to delineate the scope of application of the LCE standard in this respect would cease making the LCE standard a stand-alone standard. In addition, the seventh bullet in paragraph A.9 can be clarified by referring to the need to apply an expected loss model or to value complex financial instruments for which there are no robust market prices.

5. Accounting Firms

PriceWaterhouseCoopers

Transactions are complex or the information system and related processes relevant to the entity's financial statements are complex... - Defining characteristics of complexity which themselves refer to complexity does not support auditors in understanding what may be deemed a complex transaction or a complex information system. Many information systems in today's business environment would likely be deemed complex to some degree. Again, we believe describing what types of information system or IT packages would be considered less complex helps remove much of the subjectivity and reduces the risk of inconsistent judgements being drawn by different auditors for similar fact patterns.

The entity's IT environment or IT systems are complex... - As per previous bullet.

RSM International

certain issues in the list of prohibited entities in paragraph A9. In our view, not all special purpose entities are complex, for example a company that owns a single building. In addition, a highly integrated IT environment does not necessarily make the entity complex as these are commonly found in even quite small retail entities. We therefore recommend that the IAASB defines both special purpose entities and highly-integrated IT environment more closely to prevent entities being scoped out of ED-ISA for LCE inappropriately.

In our opinion, the Authority as set out in ED-ISA for LCE can be implemented, however we have concerns that it will not be implemented unless IAASB addresses:

7. Professional Accountancy and Other Professional Organizations

Institute of Chartered Accountants of Ghana

The Entity's IT Environment and IT System(s)

The IT organizational structure involves a dedicated IT department(s) that have structured processes, develop and implement program changes, manage access rights and are supported by personnel that have software development and IT environment maintenance skills. Alternatively, the entity may use internal or external service providers to manage certain aspects of, or IT processes within, its IT environment to meet its IT needs as indicated by the nature and extent of its business activities and related transactions and events.

The entity has numerous IT systems and applications where information is passed from one IT system/application to another with complicated data interface.

The entity's IT environment includes highly-customized or highly-integrated IT applications, including financial reporting processes or IT applications that may be integrated with other applications (such as ERP systems).

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. Operations - regulation or regulatory oversight

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Characteristic of "The entity's operations are subject to a higher degree of regulation or to significant regulatory oversight"

The field-testing showed that some LCEs operate in industries subject to regulation or regulatory oversight. It was unclear whether they would be considered “higher degree” or “significant”, making the standard inappropriate to use. Examples of entities that operate within regulated industries that otherwise have simple, less-complex operations include:

daycares;

small insurance brokers/dealers; and

entities that hold trust accounts, for example, law and insolvency firms, notaries, travel agencies, and funeral homes.

7. Professional Accountancy and Other Professional Organizations

International Federation of Accountants’ Small and Medium Practices Advisory Groups

We also believe there should be additional clarity for non-governmental organizations (NGOs) and whether they would qualify to use this standard if all other criteria are met. For example, during field testing of the authority of standard in Canada, questions arose about when regulated entities are “subject to a higher degree of regulation”. Examples of non-complex, but regulated entities include day cares, law firms or real estate agents holding trust accounts, and small insurance brokers / dealers. We believe that if all regulated entities or entities who have regulated operations are excluded, then the pool of potentially eligible entities is greatly diminished in many jurisdictions.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3a) Comments on Specific Characteristics\A9. Ownership & Oversight

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Characteristic of “Ownership and oversight structures”

The Supplemental Guidance for the Authority notes that concentration of ownership and management in a small number of individuals in an LCE is a “complexity” characteristic. However, many LCEs have concentration of ownership and management in a small number of individuals and stakeholders questioned whether this was an indicator of complexity. Additionally, stakeholders noted that LCEs may have complex structures for tax planning or business management purposes that do not impact the complexity of the audit. It is unclear how this characteristic impacts the ability of the auditor to obtain sufficient appropriate audit evidence.

Japanese Institute of Certified Public Accountants

With respect to the organizational structure (second bullet point) and oversight structures (third bullet point) listed in paragraph A.9 of the ED-ISA for LCE as qualitative characteristics, the judgment of whether the structures of the audited entity fall under these characteristics is subjective if it is left to the discretion of each audit engagement team, and this may cause variability. Therefore, it would be preferable to leave it to legislative or regulatory authorities or relevant local bodies with standard-setting authority to specifically determine what organizational and oversight structures generally fall under these qualitative characteristics in their jurisdiction. In addition, although special-purpose entities (SPEs) are cited as an example of complexity in organizational structure, we do not think it is necessary to explicitly state this because there are many cases where they are not complex.

5. Accounting Firms

MNP LLP

Organizational structure

Paragraph A.9 describes one of the characteristics of complexity as “ownership or oversight structures [that] are complex”. Oftentimes complex structures exist for the purposes of tax planning, however these are not indicative of complexity in a way that would impact our audit efforts or the needs of the users. We believe

that further clarification should be provided so it is specific that the complexity of the ownership or oversight structure is such that it impacts the complexity of the audit or that this characteristic should be removed.

PriceWaterhouseCoopers

Ownership or oversight structures are complex - It is unclear how oversight alone may reflect the underlying complexity of the entity, its operations and financial reporting i.e., the subject matter of the audit.

7. Professional Accountancy and Other Professional Organizations

Eurasian Group of Accountants and Auditors

It follows from paragraph A9 that the ED-ISA for LCE is not appropriate for auditing financial statements if the entity has a complex ownership or oversight structure. We believe additional clarification is needed to paragraph A9 to clarify where the complexity of ownership or oversight structure affects audit complexity.

Self-Regulatory Organization of Auditors Association (SRO AAS)

It follows from paragraph A9 that the ISA for LCE is not suitable for auditing financial statements if the entity has a complex ownership or supervision structure. We believe that additional clarifications should be given to paragraph A9 to clarify in which cases the complexity of the ownership structure or supervision affects the complexity of the audit and whether or not the complexity decision tree may be included in the standard.

9. Individuals and Others

ASK KSA Consulting Inc.

There are other areas where the description of the qualitative characteristics is too general and does not provide adequate guidance. For example, multiple levels and reporting lines, with many individuals involved and of itself do not make for a complex entity. Another example is what is the definition of complex ownership? It is not clear how this makes an entity complex or not complex.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3b) Too Much Judgment\Concern Over Judgment - General

4. National Auditing Standard Setters

Australian Auditing and Assurance Standards Board

The AUASB's stakeholders shared a strong preference that clearer, more objective criteria should govern the application of the proposed ED-ISA for LCE Standard.

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.

Federación Argentina de Consejos Profesionales de Cs. Económicas

We believe that sections A.8. and A.9. they are difficult to implement and highly discretionary.

We consider that the description of the qualitative characteristics that could prevent the use of the ISA for EMC for the audit of the financial statements of the entity is not sufficient to give certainty to the auditor that his decision has been correct, and could generate difficulties in opportunity to have to defend your decision in the face of a third party requirement or in the face of complex situations that do not exist or are not noticed at the beginning of the audit that will force you to rethink not only future procedures but also the adaptation of those already carried out.

Hong Kong Institute of Certified Public Accountants

Limitations through qualitative characteristics

Some of our stakeholders expressed concern that applying qualitative characteristics to determine the applicability of the proposed standard involves a high level of professional judgement and poses practical difficulty. Take for example an entity with its core business in developing IT software and infrastructures which is expected to remain inactive for the next two years with limited transactions. Arguably, the nature and extent of its business activities is complex but its inactive status indicates that its auditors would otherwise be eligible to apply ED-ISA for LCE.

Institute of Chartered Accountants of India

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.

In our view, this is an area where specific attention of IAASB is required while progressing the standard to finalization.

Qualitative characteristics are subjective and involve lot of judgments. Further, on account of these judgements we feel that the conclusions reached by one auditor may not be similar to the conclusions reached by another auditor. There has to be more specific guidance in this area.

Public Accountants and Auditors Board Zimbabwe

The qualitative characteristics leave significant room of judgement and are difficult to apply with consistency from one engagement to the next or from one auditor to the next.

5. Accounting Firms

Deloitte Touche Tohmatsu Limited

We believe that the level of professional judgment necessary when evaluating the qualitative characteristics described in the Authority to determine whether an entity could be audited under the proposed standard could lead to inconsistencies in application, and possible misuse of the proposed standard. Without additional examples in the Authority Supplemental Guidance of what entities would be considered in scope, the Authority could be open to significant interpretations and lead to situations in which either: 1) auditors more easily and inappropriately justify use of the proposed standard when in actuality the ISAs should be followed, or 2) auditors are hesitant to use the proposed standard due to concerns that they might be challenged by regulators.

ETY sas

However, as drafted, these Qualitative Characteristic 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.

Although the table below paragraph 28 of the Authority Supplemental Guide is somewhat helpful in providing examples of characteristics that may or may not be associated with an LCE, words like “complex” and “straightforward” are still used and provide the same concerns as with paragraph A9.

As such, we believe that the IAASB should consider amending the Qualitative Characteristics section (paragraphs A8-A9) of the proposed standard by clarifying what “complex”, “simple”, etc. means or using different ways to describe how the Qualitative Characteristics will influence the auditor’s decision as to whether an entity is an LCE.

Grant Thornton International Limited

The inclusion of qualitative characteristics in determining whether ISA-ED for LCE can be applied to the audit of an entity, by definition will result in an inconsistent application of the Proposed Standard. Additional material on the application of those characteristics is unlikely to alleviate such inconsistent application and will only serve to add to the complexity of determining whether it is appropriate to apply ED-ISA for LCE.

The table presented in paragraph 28 of the Supplementary Guidance for the Authority of the [Draft] Standard (the Supplementary Guidance), whilst a helpful aid to understand what constitutes qualitative characteristics, may be interpreted as a bright line as to when the standard can or cannot be applied. This may have the consequence of ED-ISA for LCE being excluded from use when its application to the audit of an entity may be appropriate. For example, in the Business Activities, Business Model or Industry section of the table, entities that are ‘start-ups’ are by default considered inappropriate to be audited under ED-ISA for LCE; however, not all start-up entities are complex in nature.

KPMG IFRG Limited

Despite the efforts of the IAASB in describing in detail the authority of the standard, we believe there is still scope for differing interpretation regarding its application, both in terms of differences in practice/ interpretation as a result of the inherent subjectivity in determining whether an entity has the qualitative characteristics of an LCE as envisaged by this standard, as well as for inconsistent interpretation/application across jurisdictions. The IAASB has attempted to address this via the “if in doubt, you are out” overriding principle, but the inclusion of qualitative factors in the entry point to the standard inevitably results in some subjectivity.

We highlight that this is different to all other standards of the IAASB (audit, review, assurance etc.), use of which is determined at a jurisdictional level and does not rely on subjective characteristics. We also

refer to our comments in our response to Questions 1a) and 13a) that, over time, certain auditors may no longer be sufficiently familiar with the full-scope ISAs to be able to make appropriate scoping determinations, as well as to our comments in our response to Question 1a) that auditors may be subject to commercial pressure to use this standard when it may not be appropriate to do so.

This subjectivity is also exacerbated by the fact that the IAASB describes, at paragraph A9, that the list of characteristics is not exhaustive, and notes that characteristics on their own may not be sufficient to enable a determination to be made.

Moore Global Network Limited

The decision regarding an entity being a LCE as proposed is based on qualitative measures, which could lead to indecision or inconsistencies in decision making amongst users as opposed to using measurable elements only.

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.

Price Bailey LLP

As noted above the qualitative characteristics are not clear enough and therefore could lead to misunderstanding, inconsistencies and challenge from regulators.

It is important that the authority is clear and unambiguous. Specific examples in the supplementary material in regard to types of accounting estimates may assist with clarifying the authority. If it is too time consuming at the planning stage to ensure you have correctly categorised is as an LCE or not, it will deter people from adopting the standard.

It is very important that it can be categorised easily and with confidence at the planning stage as transitioning during the audit would be complicated and therefore costly.

PriceWaterhouseCoopers

As noted within our response to question 3 we find the level of subjective judgement required in applying the qualitative characteristics to be too great and open to differing interpretations. The inherent subjectivity would, in our view, necessitate a robust level of risk assessment procedures to understand the entity to enable an informed judgement on the appropriateness of using the standard on a new audit engagement, which is counterintuitive.

RSM International

Auditors are generally risk averse and may err on the side of caution when presented with the qualitative characteristics as currently drafted. In addition, other auditors may stretch the qualitative characteristics to fit the criteria for using the ED-ISA for LCE.

7. Professional Accountancy and Other Professional Organizations

Accountancy Europe

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 for the same entity and this might confuse entity's management, users and the regulators.

ASSIREVI

With respect to the qualitative characteristics, in addition to that set out in our response to question 3 and as already noted in our comments on the DP, we agree with the qualitative characteristics identified as characteristics that could be commonly considered in order to define whether an entity is more or less complex. Also, we acknowledge that those characteristics are neither exhaustive nor exclusive to smaller entities and remain fairly convinced that quantitative thresholds are not appropriate in all circumstances and that professional judgement is necessarily required.

While we appreciate the usefulness of the Authority Supplemental Guide (see our response to question 5), we note that as the qualitative characteristics are - as per the proposed standard - criteria applied to exclude entities that have such characteristics from the scope of the proposed standard, an auditor's decision about such criteria taken in a certain period may differ from that of another auditor for the same entity. This would affect the expectation about the consistent application of the proposed standard. In addition, the discretionary and highly subjective nature of the auditor's assessment could be questioned ex post as a result of any subsequent events and/or additional facts.

Chamber of Auditors of the Czech Republic

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 for the same entity and this might confuse entity's management, users and the regulators.

CPA Ireland

In determining appropriate qualitative characteristics at individual engagement level CPA Ireland considers that this will be challenging for auditors to navigate the current approach, particularly in "borderline" cases. It would be useful to have some application material in this regard.

Also, the assessment of the application of qualitative characteristics and their permitted use may be challenging for regulatory authorities.

European Federation of Accountants and Auditors for SMEs

there are many of these and inevitably their application will be highly subjective. While we appreciate the effort taken to develop, articulate and describe these criteria we suspect the degree of subjectivity may mean they are not implementable. While the LCE concept is conceptually appealing and in keeping with the notion that ISAs underpin a risk-based audit LCE has many drawbacks. LCE is a new and unproven concept. LCE is not a sector. LCE is highly subjective and hard to define.

Finnish Association of Authorised Public Accountants

Determining whether an engagement includes complex characteristics is a matter of professional judgement. The interpretation may vary a lot between auditors, auditor oversight bodies and stakeholders in different jurisdictions, which may cause inconsistencies in the application of the standard. What one considers complex is not complex to the other (e.g. Black & Scholes model, cash flow forecasts, goodwill or POC).

Institute of Certified Public Accountants of Cyprus

In addition, it is risky (at least from the very beginning) to leave it to the practitioners to decide whether a company is an LCE or not as it involves a lot of judgement. Practitioners also have the policies and procedures methodologies they follow. It could be the case that they are happy with the methodology already established for a company and switching to the ISA for LCE would seem more burdensome and costly (passing the cost on to SMEs) than using the ISAs.

Korean Institute of Certified Public Accountants

We agree with the overall qualitative characteristics proposed in the ED-ISA for LCE. However, as noted in the answer to Question 3, there are significant concerns that current qualitative characteristics are abstract and hard to judge. Such concerns don't seem to be resolved even by the supplemental guidance. We want the qualitative characteristics to be revised to make them more specific, hence less room for exercising judgment

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

However, as drafted, these Qualitative Characteristic 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.

Polish Chamber of Statutory Auditors Warsaw (Regional Branch)

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.

It should be clear to which engagements the standard is applicable. The list of orders should be closed. It should not be possible to rely on judgment.

Society of Certified Accountants and Auditors of Kosovo (SCAAK)

Qualitative characteristics – there are many of these and inevitably their application will be highly subjective. While we appreciate the effort taken to develop, articulate and describe these criteria we suspect the degree of subjectivity may mean they are not implementable. Therefore, we believe that more guidelines are needed to auditors when assessing these characteristics.

South African Institute of Professional Accountants

Limiting Use through Qualitative Characteristics

If the use of the [draft] standard is not prohibited by the specific prohibitions, the auditor have to exercise judgement and consider the qualitative characteristics in determining if the standards is appropriate for the entity.

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.

Professional judgment is used in determining whether the entity exhibits the qualitative characteristics of a less complex entity and the [draft] standard is therefore appropriate to use.

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.

8. Academics

Argentine institute of Auditing Professors

(b) On the other hand, the analysis of qualitative characteristics is highly subjective and will depend on the auditor's professional criteria.

9. Individuals and Others

ASK KSA Consulting Inc.

The Authority currently states there are qualitative characteristics that if met, it would be inappropriate for an audit to be undertaken using the ED-ISA for LCE. There are certain areas within this list that require clarification.

Complex matters or circumstances requires extensive professional judgement. Even if an auditor documents this professional judgement and concludes they are within the Authority of the standard, what is the impact if a practice inspector arrives at a different conclusion? If that is the case would the auditor be required to re-perform the audit in accordance with ISA. The implications and cost of this to both the entity and the auditor is significant.

The first bullet of A.9 states that if the entity's business activities result in pervasive risks that increase the complexity of the audit then the standard may not be used. However, as the introduction is written, it states that the standard is inappropriate if an entity exhibits one or more of the listed characteristics. Is that to suggest if that if any of the characteristics are met, the standard cannot be used. If more than one characteristic, the question arises as to how many more. Or, if only one, then does that automatically mean the standard cannot be used?

There are other areas where the description of the qualitative characteristics is too general and does not provide adequate guidance. For example, multiple levels and reporting lines, with many individuals involved and of itself do not make for a complex entity. Another example is what is the definition of complex ownership? It is not clear how this makes an entity complex or not complex.

Being an auditor requires the use of professional judgment throughout an audit but there are times where less professional judgement may be better.

We recommend that the Authority is very narrow and while professional judgement is always required the use of professional judgement as to when or not to apply the standard is lessened. By tightening up the Authority, this also allows for the elimination of many of the challenges faced by auditors as further explained throughout our response.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3b) Too Much Judgment\Consequences of Judgment (View with Q3b)

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

AASB views and recommendations

Considering the feedback from stakeholders and field-testing, we have the following concerns with the Authority being open to interpretation and requiring significant professional judgment in assessing whether an entity exhibits the qualitative characteristics:

ED-ISA for LCE could be used when inappropriate. The ambiguity in the Authority leaves room for practitioners to conclude on the use of the standard incorrectly. There is also a risk of practitioner bias to continue to apply the separate standard when it is necessary to transition to the ISAs. Therefore, there may be a negative impact on audit quality.

Inconsistency in practice. What may be determined as complex by one auditor may not be complex for another auditor due to their experience. Therefore, practitioners may arrive at different conclusions regarding the use of the standard for similar entities, and, as a result, the IAASB's goal to promote a more consistent application of the auditing standards to audits of LCEs may not be achieved.

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

Institute of Certified Public Accountants of Cyprus

In addition, it is risky (at least from the very beginning) to leave it to the practitioners to decide whether a company is an LCE or not as it involves a lot of judgement. Practitioners also have the policies and procedures methodologies they follow. It could be the case that they are happy with the methodology already established for a company and switching to the ISA for LCE would seem more burdensome and costly (passing the cost on to SMEs) than using the ISAs.

9. Individuals and Others

ASK KSA Consulting Inc.

The Authority currently states there are qualitative characteristics that if met, it would be inappropriate for an audit to be undertaken using the ED-ISA for LCE. There are certain areas within this list that require clarification.

Complex matters or circumstances requires extensive professional judgement. Even if an auditor documents this professional judgement and concludes they are within the Authority of the standard, what is the impact if a practice inspector arrives at a different conclusion? If that is the case would the auditor be required to re-perform the audit in accordance with ISA. The implications and cost of this to both the entity and the auditor is significant.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3b) Too Much Judgment\Eye of the Beholder

3. Regulators and Audit Oversight Authorities

Independent Regulatory Board for Auditors (IRBA)

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 such an 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.

5. Accounting Firms

Azets Audit Services

(c) One of the issues with qualitative characteristics is that they are in the eye of the beholder. One person's complex ownership structure, accounting estimate methodology or sector may be another person's bread and butter. This may lead to quantitative override at the Jurisdictional or Firm level. This is not in and of itself a fatal flaw, but it may impact on the standard's application at the engagement level and need for additional guidance to facilitate appropriate adoption.

(

BDO International

Further clarification is needed on what constitutes 'complex ownership', 'a complex transaction', or 'complex accounting'. From whose perspective is the complexity of the ownership, transaction or accounting assessed? If management routinely processes a particular type of transaction, it may not seem complex to them, whereas it would be to an entity that seldom processes such transactions. To an auditor who regularly audits share-based payments, encountering share-based payments during the audit is unlikely to appear 'complex'; but to an audit firm who has not dealt with them before, it may well be complex. We appreciate that examples can be provided through implementation guidance, but the underlying principles should be well defined in the LCE standard.

ETY sas

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.

Mazars

Using "qualitative characteristics" in a consistent way is very subjective:

For the qualitative characteristics the auditor is expected to use professional judgement.

There might be instances where one auditor in year 1 and a successor auditor in year 2 come to different conclusions regarding the complexity assessment. In rare situations this might confuse the different stakeholders.

What can be a challenge is the possible divergence between the auditor who decides to use the ISA for LCE and the client who is reluctant as he has a covenant within the bank agreement where it is noted to have a report under ISA.

We believe it will be rare but probably more important at the start of the implementation: there might be also facts or circumstances appearing throughout the year that makes the ISA for LCE not applicable any longer. How will the transition be done? Especially, what would happen when the entity has a complex issue in one year (so not within LCE standard scope) but no for the other years (can be within LCE scope) – how would this transition between ISA and LCE happen?

Audit firms and auditors may define “complexity” differently, especially for IT complexity and estimates, thereby creating variations between application of the LCE standard. Hence the need to update the IFAC SME guide to ensure consistency for quality. If the auditor is required to make too many interpretations, he may be reluctant to use a new framework and would go rather use an accepted framework which is current set of ISA.

PriceWaterhouseCoopers

The entity’s business activities, business model or the industry in which the entity operates results in pervasive risks that increase the complexity of the audit - This represents a highly judgemental determination that will be influenced by personal experiences of financial statement preparers and auditors with regard to perceptions of risk and complexity. We believe directly describing attributes of an entity’s operations that are considered to be less complex is easier to visualise.

7. Professional Accountancy and Other Professional Organizations

Accountancy Europe

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 for the same entity and this might confuse entity’s management, users and the regulators.

ASSIREVI

While we appreciate the usefulness of the Authority Supplemental Guide (see our response to question 5), we note that as the qualitative characteristics are - as per the proposed standard - criteria applied to exclude entities that have such characteristics from the scope of the proposed standard, an auditor’s decision about such criteria taken in a certain period may differ from that of another auditor for the same entity. This would affect the expectation about the consistent application of the proposed standard. In addition, the discretionary and highly subjective nature of the auditor’s assessment could be questioned ex post as a result of any subsequent events and/or additional facts.

Association of Practising Accountants

In A9, at the 7th bullet point it refers to “complex methods” with accounting estimates. There could be a number of different interpretations of the types of accounting estimates which would meet that definition, as different firms / audit engagement partners may classify “complex methods” differently. Something that may be seen as complex to one audit partner may seem less complex to someone who specialises in a particular area.

Finnish Association of Authorised Public Accountants

What one considers complex is not complex to the other (e.g. Black & Scholes model, cash flow forecasts, goodwill or POC). Therefore, we think that it is useful to give as many practical examples as possible in the EEM or Authority Supplemental Guide. The examples should include not only the most obvious cases but also those in the “grey area”. National guidance is needed so that typical entities and national characteristics as well as laws and regulations can be taken into account. National accounting standards may not include as many complex (or even non-complex) accounting estimates or fair value calculations as IFRS, and this should have an effect on the consideration of complexity at national level.

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

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.

Pan-African Federation of Accountants (PAFA)

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.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3c) Additional Indicators of Complexity

3. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies

In the essential explanatory material (EEM) to paragraph 1.2.1, it is mentioned that if an Engagement Quality Review (EQR) is required, ISQM2 will be applicable. We question whether having an EQR indicates that this draft standard may not be appropriate. Usually, if the audit firm decides on a voluntary basis to have an EQR, it could be because a particular risk has been identified resulting from the complexity of the audit, as illustrated by the examples provided in paragraph A134 of ISQM 1. Therefore, having an EQR could be added to the list of indicators that the auditor should take into consideration when identifying if the use of the ISA for LCE is or remains appropriate.

Irish Auditing and Accounting Supervisory Authority

The essential explanatory material (EEM) to paragraph 1.2.1 states that if an Engagement Quality Review (EQR) is required, ISQM2 will be applicable. We question whether the requirement for an EQR indicates that use of the LCE standard may not be appropriate. Usually, if the audit firm decides to have an EQR on a voluntary basis, it is because a particular risk has been identified resulting from the complexity of the audit, as illustrated by the examples provided in paragraph A134 of ISQM 1. Therefore, having an EQR could be added to the list of indicators that the auditor should take into consideration when identifying if the use of the ISA for LCE is or remains appropriate.

4. National Auditing Standard Setters

American Institute of Certified Public Accountants

If the IAASB disagrees with this recommendation and, instead, believes that the preceding matters (and other circumstances that were not contemplated in the design of the Exposure Draft) are prima facie indicators of complexity, we recommend that the Authority Document be revised to include a list of all such circumstances so that the auditor is aware of the limitations on the use of the proposed standard prior to the commencement of the engagement.

The last circumstance is specifically troublesome as many LCEs prepare financial statements in accordance with a special purpose framework, such as the modified cash basis or income tax basis of accounting. Many such frameworks are inherently less complex than a general-purpose framework such as International Financial Reporting Standards (IFRS). The International Accounting Standards Board implicitly acknowledges the complexities included in IFRS with the issuance of IFRS for Small- and Medium-Sized Entities.

While, as noted above, it is important to articulate a clear definition of an LCE, we do not believe that group audits or special purpose frameworks should be categorically excluded from that definition. The reference to these and other matters that are not prima facie indicators of complexity could be conditional. That is, the requirement could be such that when the auditor encounters such issues during the audit of the financial statements of an LCE, then certain requirements would apply. When these types of circumstances exist, the inability to perform the audit in accordance with the Exposure Draft will result in a significant impediment to adoption.

. While group audits are specifically excluded from the Authority Document, there are other circumstances that are not addressed in the Exposure Draft, which implies that they are potentially perceived to be an indication that the entity is complex:

the auditor's communication of key audit matters in the auditor's report when the auditor is engaged to do so,

use of internal audit, and

financial statements prepared in accordance with a special purpose framework.

5. Accounting Firms

KPMG IFRG Limited

certain matters, such as complex financing arrangements; complex transactions, and complex accounting estimates, are specifically identified as proxies for complexity within the authority section of the standard, whilst other areas where there are matters that may involve complexity, such as matters that could be assessed as significant risks and/or require the auditor to exercise significant professional judgement, including the matters listed in our response to Question 3c) are not also explicitly identified as potential sources of complexity; and the characteristics described are entity-specific, however, complexity may be driven by factors that are external to the entity, e.g. the macro-economic environment, which the standard does not currently address.

In connection with this, we note that the IAASB has specifically identified, within the authority section of the standard, certain characteristics which are considered to involve complexity, such as complex financing arrangements; complex transactions, and accounting estimates that are subject to a higher degree of estimation uncertainty, or when the measurement basis requires complex methods, as “proxies for complexity”. We understand the IAASB intends for the term “complexity” to be interpreted somewhat broadly, as indicated by the fact that one of the characteristics of complexity in A9 is that the entity’s accounting estimates are subject to a higher degree of estimation uncertainty (and the Supplemental Guidance for the Authority of the Standard notes that accounting estimates that do not require significant judgments are less complex, the implication being that estimates with significant judgments are considered complex). This indicates that factors such as subjectivity, [estimation] uncertainty and susceptibility to management bias are also considered proxies for “complexity”. Consequently, the term complexity appears to encompass most, if not all, matters that could be assessed as significant risks and/or require the auditor to exercise significant professional judgement. Therefore, we question why other areas, in addition to those specifically identified by the IAASB, where there are matters that may give rise to “complexity” in the audit are not also explicitly described. For example, the following could also involve complexity: significant risks relating to matters other than complex financing arrangements, complex transactions and complex estimates, including fraud risks; management’s going concern assessment when events or conditions that may cast significant doubt on an entity’s ability to continue as a going concern have been identified; significant unusual transactions outside the normal course of business; application of the applicable financial reporting framework to accounting matters that are contentious or highly subjective, or matters for which management has involved a management’s expert, and matters for which the auditor determines they need an auditor’s expert.

We believe it would be unusual for the above matters to arise on an audit and not involve a reasonable degree of complexity. We are concerned that by not explicitly identifying these matters in the authority section as potential sources of complexity, and by retaining applicable requirements relating to these matters from the full-scope ISAs, this could result in significant uncertainty (and differing interpretations) as to whether, and under what circumstances, it is appropriate to conduct an audit using the LCE ISA when one or more of these matters arises.

PKF International Limited

Further to our comments in 3(b) above, there are four additional scenarios which we believe the IAASB should consider for possible inclusion as a specific prohibition in ED-ISA for LCE:

The engagement is a first-year audit of the entity

The audit engagement team determines that it needs to use the work of an auditor’s expert

There is a material uncertainty over going concern (including where identified as part of the initial engagement activities)

The engagement requires an Engagement Quality Control Reviewer

Each of 1 – 4 above are common matters which we expect will affect many engagements performed under the proposed standard. Each would lead to additional complexity for an audit, including complexity in terms of the underlying circumstances and conditions of the audit, as well as increased complexity due to the additional audit procedures and audit file documentation that will be necessary to respond to each of these circumstances.

On item 1 above - for a first-year audit, there may be complexities affecting the entity and the audit which are not fully apparent to the engagement team until an audit has been completed. In our view, it would be appropriate to restrict the use of ED-ISA for LCE on a first-year client engagement until at least one audit engagement has been performed for that entity. Such a delay should enhance the engagement team's ability to form an appropriate understanding of the circumstances affecting the complexity affecting the engagement.

On item 2 above - our concern is that the need to utilize an auditor's expert may demonstrate that the engagement causes a level of complexity which exceeds the core competencies of the engagement team. The additional audit effort and documentation requirements in such a circumstance also add to the overall level of complexity of the engagement.

On item 3 above – where a material uncertainty due to going concern has been identified during the audit process, there is a significantly higher likelihood of more complex procedures being required, including review of forecasts and estimates, a deeper level of understanding of funding and loan covenants and greater levels of judgement and scepticism will likely need to be applied.

On item 4 above – where a firm has appointed an Engagement Quality Control Reviewer (EQCR) to an engagement, this can be indicative of a higher level of complexity in the audit engagement compared to other audit engagements which don't require appointment of an EQCR.

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).

6. Public Sector Organizations

Office of the Auditor General of Alberta

Furthermore, there are multiple characteristics of an audit that indicate that the entity may not be a less complex entity. These characteristics are not incorporated into the prohibitions and the ED incorporates requirements when these characteristics are present. For example, if a firm determines the audit requires an EQCR or the audit team determines it is necessary to use an external expert. Individually, each of these factors is permitted under ISA for LCE. The board should re-evaluate if these individual characteristics, individually and cumulatively, should be permitted for a less complex entity. In our view, entities that require an EQCR, reliance on management's expert or reliance on an auditor's expert can be excluded from the ISA for LCE standard because if these are present, the entity is likely not a less complex entity.

Swedish National Audit Office

To ensure that the standard is applicable in the public sector we would like to suggest that you clearly state that any public sector auditor such as supreme audit institution may define when the standard is applicable or not depending on the specific audit environment. We would suggest avoiding using expressions and wordings which could lead to the standard not being applicable in the public sector. Terminology used should be defined and clear.

In addition, we would suggest that the standard to a larger extent focuses on disqualifying entities with significant risk. This could be done under the qualitative factor section (A8-A9) by stating that entities with for example the following risks should be excluded:

- significant risks in general and especially risk for accounting estimates
- potential risks for going concern, fraud
- large and complex transactions with complex accounting principles.

7. Professional Accountancy and Other Professional Organizations

Confederation of Swedish Enterprise

We believe that an alternative is to assess the applicable accounting standards for the entity instead of focusing on the accounting of a specific item. This means that local GAAP might have an impact on the assessment of complexity. If the entity e.g. applies an accounting standard specially designed for SMEs, this could be an indication that the accounting is less complex.

Korean Institute of Certified Public Accountants

We agree with the overall qualitative characteristics proposed in the ED-ISA for LCE. However, as noted in the answer to Question 3, there are significant concerns that current qualitative characteristics are abstract and hard to judge. Such concerns don't seem to be resolved even by the supplemental guidance. We want the qualitative characteristics to be revised to make them more specific, hence less room for exercising judgment. For example, it may be useful to consider following options.

Refining the qualitative characteristics proposed in A.9 in a way that they can be more intuitive or quantifiable (e.g., involving general risks that add to complexity of audit → multiple products/services and geographically decentralized production/sales) or adding such characteristics (e.g., presence of internal audit function)

Presenting the characteristics of auditors or audit engagement (e.g., audit hours, use of external experts) as proxies for complexity as audit efforts increase if an entity has a higher level of complexity

South African Institute of Chartered Accountants (2)

Another consideration is the annual revisiting of whether an entity still “meets” the definition of a LCE and vice versa and the allowance for an auditor not to be prohibited from using the LCE standard if this standard could not have been used in the previous years on a specific entity as the nature and circumstances of an entity may change from time to time.

Entities trading in more than one currency or jurisdiction should also be considered as more complex, as per the list in para A10.

The LCE standard should also acknowledge dormant entities to be LCEs and to then further simplify the audit process with regards to dormant companies. Dormant entities are basically shells and have no activity or transactions. Practically, the engagement documentation could be reduced to a few working papers where the auditor corroborates that the entity's status is indeed dormant and if corroborated then to only complete one planning, one fieldwork and one concluding working paper as no risks exist at a dormant company other than the reporting thereof in accordance with the relevant financial reporting framework.

Paragraphs A 9 – A10: With the purpose of the LCE standard in mind [i.e. to simplify and increase efficiency and not to duplicate effort] as well as the extensive professional judgment that is to be applied in deciding on whether the use of the LCE standard is appropriate for a specific entity there could be a need to include another annexure to the LCE standard of a “qualitative characteristics” decision tree that is to be completed by the auditor as part of pre-engagement phase and on which it is concluded whether the LCE standard can be used or not. Such an annexure should allow for documented support for responses to the questions posed in the decision tree to each of the relevant qualitative characteristics.

In the South African context consideration would need to be given to aspects such as the calculated Public Interest (PI) score, i.e. a higher PI score (above a specified threshold) could potentially lead to a more complex entity. The criteria used by the local audit regulator (The Independent Regulatory Board for Auditors) for inspections on the annual Assurance Work Declaration to determine whether an entity is a high risk or a low risk can also be used. For example, the LCE standard could be prohibited for entities classified as high risk in the declaration and applicable for low risk entities.

Regulators in other jurisdictions may have similar requirements and assessments in terms of identifying high risk versus low risk audits and these principles may be included in the qualitative characteristics

8. Academics

Accounting and Finance Association of Australia and New Zealand

We also note our response to Question 22 and Question 1a and suggest the possibility, depending on the direction that the IAASB take on group audits and the standalone nature of the standard, of including the use of component auditors and the need to refer to the full suite of standards for guidance as indicators, but not definitive of, complexity that may render the standalone standard inappropriate.

To further inform an understanding of the factors that may be indicative of complexity, we examined the audit fees of Australian companies. Audit fees are a function of the resources necessary to achieve effective audit outcomes and likely depend on the inputs and their associated costs (Knechel and Sharma 2012). To the extent that these inputs are indicative of complexity, there should be an association between complexity and audit fees.

Due to data limitations, we restricted this analysis to listed companies. While we acknowledge that listed companies are, as the proposed standard is currently drafted, scoped out of the standard, the analysis is informative in understanding the correspondence between entity characteristics and complexity. Employing data for ASX-listed companies from 1995 to 2021, the analysis reveals that companies paying higher audit fees, and therefore indicative of greater complexity, have significantly higher total assets, a greater number of geographic and business segments, have foreign operations, and have higher levels of inventory and receivables. We have not analyzed data in other jurisdictions but have no reason to believe that results would be meaningfully different. On the basis of this analysis, the indicators of complexity appear appropriate, but we do note that a large proportion of the listed entities in our sample appear to be less complex, and we refer the IAASB to our comments in response to Question 4a. We provide further details of this analysis in Appendix B.

We note research that speaks to dimensions of complexity (e.g., Anderson 1999; Dooley 2002) and remind the IAASB of the multidimensional character of complexity. This, in turn, highlights the difficulty in establishing rules based bright line criteria for scoping entities into and out of the proposed standalone standard. Therefore, we recommend that the authority be focused on qualitative criteria allowing for professional judgment to take into account idiosyncratic auditor, client, and jurisdictional circumstances. A large body of research in auditing (and corporate governance) has considered factors that make an audit more complex, usually in order to control for differences among clients. The most commonly used measures for firm complexity in the research literature are; number of subsidiaries, number of geographic or business segments, number / percentage of foreign subsidiaries, percentage of foreign assets, foreign income/sales, national and multinational operations, auditor-related factors, firm age, merger and acquisition activities, ownership structure, technology-related issues, and labor intensity (number of employees). We reference the extensive literature supporting each of the measures in Appendix A to our submission.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3d) Complexity isn't just driven by the entity

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

We also note that the characteristic “Transactions are complex or the information system and related processes relevant to the entity’s financial statements are complex such that data collection and processing involves complex accounting or calculations” combines two different factors (i.e., (i) transactions and (ii) information systems and related processes)”. We suggest that the IAASB separate these so that there is a qualitative characteristic that deals with complex transactions and another that deals with complex information systems and related processes.

5. Accounting Firms

KPMG IFRG Limited

the characteristics described are entity-specific, however, complexity may be driven by factors that are external to the entity, e.g. the macro-economic environment, which the standard does not currently address.

MNP LLP

Complexity of users vs. complexity of entity

We believe that the authority of the ISA for LCE standard combines the complexity of the entity with the complexity of the userbase. As ISA for LCE is designed to achieve a level of reasonable assurance, regardless of the user. It should not matter who the users are or how many there are. While increased users (e.g., more widely held, publicly traded) is an audit consideration, this isn’t a characteristic of the entity itself and should not factor into the entity’s complexity determination.

7. Professional Accountancy and Other Professional Organizations

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

Some of our stakeholders raised concerns that the standard currently includes too many prohibitions which could lead to confusion when considering whether a company can be scoped in. An example raised is in the case of a farm with a number of owners within a family structure which could be scoped out because of ownership, regardless of the fact that the farm operations are not complex, making it confusing as to why complexity refers back to users. Using the same example, if a farm is on First Nation’s reserved land, an indigenous community in Canada, that is likely to be excluded because of its public interest characteristics irrespective again, of whether the entity is a simple farm. We therefore recommend that the IAASB takes into consideration these concerns and explore whether the number of prohibitions can be reduced focusing on the substance of complexity.

Institute of Chartered Accountants of Namibia

The standard and the authority of the standard are aimed at entities that are less complex and can therefore use the draft standard. The draft standard currently allows for instances where entities with certain complexities can still use the draft standard if the assessment by the auditor is that the draft standard remains appropriate.

We believe that this approach ignores audit risk, such as cases where, despite the lack of complexity, the risk of material misstatement and the risk that the auditor does not identify the misstatements remains higher. In these cases, the complexity may be increased however the draft standard would not necessarily be appropriate. Examples of such cases include:

Where substantive procedures alone are insufficient.

Where the audit report includes significant “Other legal and regulatory reporting requirements”.

Any other instances where audit risks are identified in the client and engagement acceptance procedures. Instances where the nature of the entity results in significant inherent risks which increase audit risk. Where reliance is required on complex IT systems or significant and complex computer-assisted audit techniques. This differs from the current authority because where there is a complex IT system, it's an indicator of complexity, however, if the systems are not relied on for the audit, the draft standard should still apply.

Conversely, there may be instances where entities are more complex and cannot, therefore, use the draft, but the audit risk remains low. In addition, there may be cases where the users of the financial statements are limited and the public interest is very low or even zero. In these cases, despite some complexity, the audit risk is low. For example, where substantive tests of detail alone are sufficient, where external confirmations alone are sufficient etc. Examples of such cases include:

Where the audit can be performed purely with substantive procedures for example where the figures can be confirmed with external confirmations or vouched to simple rental agreements or supporting documentation. Complex valuations where the valuations are performed by appointed valuers. The audit work would be limited to evaluating the expertise etc. of the valuator.

We recommend changing the approach to be aimed at “Less complex audits” rather than “less complex entities”. We believe the authority should be based on audit risk rather than the entity's complexity.

Korean Institute of Certified Public Accountants

Refining the qualitative characteristics proposed in A.9 in a way that they can be more intuitive or quantifiable (e.g., involving general risks that add to complexity of audit → multiple products/services and geographically decentralized production/sales) or adding such characteristics (e.g., presence of internal audit function)

Presenting the characteristics of auditors or audit engagement (e.g., audit hours, use of external experts) as proxies for complexity as audit efforts increase if an entity has a higher level of complexity

We agree with the overall qualitative characteristics proposed in the ED-ISA for LCE. However, as noted in the answer to Question 3, there are significant concerns that current qualitative characteristics are abstract and hard to judge. Such concerns don't seem to be resolved even by the supplemental guidance. We want the qualitative characteristics to be revised to make them more specific, hence less room for exercising judgment. For example, it may be useful to consider following options.

South African Institute of Chartered Accountants (2)

Paragraphs A 9 – A10: With the purpose of the LCE standard in mind [i.e. to simplify and increase efficiency and not to duplicate effort] as well as the extensive professional judgment that is to be applied in deciding on whether the use of the LCE standard is appropriate for a specific entity there could be a need to include another annexure to the LCE standard of a “qualitative characteristics” decision tree that is to be completed by the auditor as part of pre-engagement phase and on which it is concluded whether the LCE standard can be used or not. Such an annexure should allow for documented support for responses to the questions posed in the decision tree to each of the relevant qualitative characteristics.

In the South African context consideration would need to be given to aspects such as the calculated Public Interest (PI) score, i.e. a higher PI score (above a specified threshold) could potentially lead to a more complex entity. The criteria used by the local audit regulator (The Independent Regulatory Board for Auditors) for inspections on the annual Assurance Work Declaration to determine whether an entity is a high risk or a low risk can also be used. For example, the LCE standard could be prohibited for entities classified as high risk in the declaration and applicable for low risk entities.

Regulators in other jurisdictions may have similar requirements and assessments in terms of identifying high risk versus low risk audits and these principles may be included in the qualitative characteristics

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3e) Describe what is less complex not complex

3. Regulators and Audit Oversight Authorities

Independent Regulatory Board for Auditors (IRBA)

Further, consideration may also be given to what an LCE is, as opposed to focusing on what it is not.

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

We suggest the following solutions to address these concerns:

What stakeholders told us

For 9 of the audit files field-tested, practitioners told us that the assessment of the qualitative characteristics is open to interpretation and requires significant professional judgment.

Specifically, they noted that, because “less complex” is not defined, it is not clear in the Authority how the ability to use ED-ISA for LCE may be impacted by:

elements of complexity commonly encountered in the operations and financial statements of LCEs, such as those related to accounting estimates; and
the presence of more than one “complexity” qualitative characteristic exhibited by an entity.

Clarify the Authority to address common complexities more clearly. The Authority should clarify what “less complex” means. Most entities have accounting estimates. Whether such estimates are subject to a higher degree of estimation uncertainty is subjective. We believe that there are some complexities that are common in LCEs, and their presence should not make the standard inappropriate to use.

5. Accounting Firms

BDO International

As drafted, the ‘qualitative characteristics’ paragraphs effectively state that an entity is not a ‘less complex entity’ if it exhibits complexity. (A.8) This does not help an auditor (or regulator) form a justifiable professional judgment about whether an entity was in scope of the standard or not. A.9 tries to go into more detail, but again defines a less complex entity by what it is not. For example, if an organisational structure is ‘not simple’, it is deemed ‘complex’.

PriceWaterhouseCoopers

As noted in our response to question 3(e) and above, we therefore recommend rearticulating characteristics of complexity by instead describing characteristics and examples that are deemed to represent or be indicative of less complexity rather than complexity.

Refining the proposals to meet expectations and minimise unintended consequences

To address our concern over the potential breadth of application, and enable further tailoring of the requirements within the proposed standard appropriate to the nature and circumstances of LCEs, we believe the standard needs to be targeted at a more defined population of entities, taking into account both complexity and size. We believe that this can be achieved through a combination of two changes within the Authority:

Refocusing the qualitative characteristics on those that are commonly associated with attributes of an LCE, rather than describing characteristics of complexity that would indicate use of the standard is not appropriate. This would drive a more conscious determination of whether the entity is truly considered to be small and less complex and that it was therefore appropriate to apply the LCE standard rather than the ISAs; and

We find the “green tick” examples described in the supplemental guidance on the Authority to be more compelling and persuasive in guiding auditors. They describe characteristics of a less complex entity. We recommend replacing the qualitative characteristics that describe what makes an entity “complex” with these direct statements about the characteristics typical of an entity for which use of the standard is appropriate.

The additional examples of characteristics that may indicate complexity could be retained as a supplemental guidance appendix to the standard. We provide additional comments in appendix 3.

RSM International

The qualitative characteristics could be clarified by incorporating the existing definition of a smaller entity from the glossary in existing IAASB Handbook. “An entity which typically possesses qualitative characteristics such as: (a) concentration of ownership and management in a single or small number of individuals; and (b) one or more of the following: (i) straightforward or uncomplicated transactions; (ii) simple record-keeping; (iii) few lines of business and few products within business line; (iv) few internal controls; (v) few levels of management with responsibility for a broad range of controls; or (vi) few personnel, many having a wide range of duties.”

7. Professional Accountancy and Other Professional Organizations

Chartered Accountants Ireland

With regard to paragraph A.8. which sets out that it would be inappropriate to use the standard if an entity exhibits complex matters or themes and matters that indicate the existence of complexity, but the standard does not set out with sufficient clarity what is considered complex or a set of factors which indicate its presence.

Institute of Certified Public Accountants of Cyprus

We are concerned about the qualitative nature of the requirements rather than having quantitative requirements as a starting point as it leaves a lot of room for auditor’s judgement that will likely lead to widely varying interpretations, and challenge by regulators. We understand that it would have been difficult for the IAASB to develop quantitative characteristics as this standard is designed to be applied globally. However, we encourage the IAASB to introduce a three-step approach:

Prohibit the use of the standard for listed entities, or entities which meet one of the criteria specified in paragraph A.7 point (c).

Assess the entity under quantitative criteria, i.e., Limit the use of the standard to small companies, and this is to be defined at a jurisdictional level.

Assess the company’s complexity, i.e. In cases whereby a small company is a complex company then it would not be able to be audited under this standard. The entity’s complexity is to be assessed under qualitative criteria by placing the focus on characteristics that are typical to an LCE and that would render applying the standard appropriate rather than delineating features of complexity that would render the application of the standard inappropriate.

If the above-mentioned process is not possible to be implemented, we encourage the IAASB to add one more paragraph making it clear that legislative or regulatory authorities or relevant local bodies with standard setting authority in individual jurisdictions are allowed to apply quantitative characteristics if they consider these to be more appropriate than applying the paragraphs in the ISA for LCE that refer to qualitative characteristics. We note that IAASB itself in pg.6 refers to the number of SMEs being more than 90% across the world implying (not intentionally perhaps) that SMEs will most likely be LCEs.

In addition, it is risky (at least from the very beginning) to leave it to the practitioners to decide whether a company is an LCE or not as it involves a lot of judgement. Practitioners also have the policies and procedures methodologies they follow. It could be the case that they are happy with the methodology already established for a company and switching to the ISA for LCE would seem more burdensome and costly (passing the cost on to SMEs) than using the ISAs.

Malta Institute of Accountants

Clarity is being sought with respect to the following:

the definition of ‘Less Complex Entities’. The qualitative characteristics are based on when an entity is not considered not to be a less complex entity on the basis of complexity rather on what is a less complex entity. In our view, defining what is a less complex entity is critical. We feel that there is ambiguity in this regard. The fact that the Standard does not try to narrow down which entities are captured (rather than what is not captured) may actually result in ‘large’ private entities being captured. Having such a broad scope makes it more difficult to simplify certain aspects given the varying nature of the entities that could otherwise

be eligible. If the entities that are captured had to be narrowed further, it may be easier to simplify certain processes and procedures within the proposed Standard.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3f) Also Consider Aggregate Impact

4. National Auditing Standard Setters

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

With respect to the qualitative characteristics, we note our comments to 3 (c) above on the clarity of paragraph A.9 and the need to deal with circumstances not covered by the LCE standard. We also believe that clarification is required that the existence of a qualitative characteristic may not give rise to complexity on its own, but that the aggregate impact of characteristics needs to be considered by the auditor when considering the appropriateness of using the LCE standard.

6. Public Sector Organizations

Swedish National Audit Office

The circumstances in paragraphs A8–A9, describing the qualitative factors, are quite many. We think that there should be some additional clarification where the auditor needs to consider an overall conclusion taken all the factors into consideration.

7. Professional Accountancy and Other Professional Organizations

Accountancy Europe

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 the ISA for LCE.

Belgian Institute of Registered Auditors (IBR-IRE)

Although the proposed standard indicates “the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the draft ISA for LCE for that entity”, we believe that this statement should receive a more prominent place in the Authority.

Chamber of Auditors of the Czech Republic

It should be emphasised that existence of one complex qualitative characteristic (especially in the area of estimates) 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 the ISA for LCE.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3g) Comments on Language\A8 & A9 Drafting Clarifications

5. Accounting Firms

Price Bailey LLP

Paragraph A8 starts by explicitly stating that LCE would be inappropriate if an entity exhibits the bulleted characteristics, but ends by stating that the bullets are merely indicators of, or proxies for, issues the ISA for LCE was not designed to address.

It's unclear whether the two bullets are to be taken together or individually (suggest you insert 'and' or 'or' after the first bullet).

PriceWaterhouseCoopers

Further to our response to part (a), we do not believe the characteristics and guidance described in paragraphs A8 and A9 alone are sufficient to drive consistent judgements.

7. Professional Accountancy and Other Professional Organizations

Association of Practising Accountants

Paragraph A8 starts by explicitly stating that using the LCE standard would be inappropriate if an entity exhibits the bulleted characteristics, but ends by stating that the bullets are merely indicators of, or proxies for, issues the ISA for LCE was not designed to address.

It is also unclear whether the two bullets in this paragraph are to be taken together or individually (worth inserting 'and' or 'or' after the first bullet).

Chartered Accountants Ireland

With regard to paragraph A.8. which sets out that it would be inappropriate to use the standard if an entity exhibits complex matters or themes and matters that indicate the existence of complexity, but the standard does not set out with sufficient clarity what is considered complex or a set of factors which indicate its presence.

Institute of Chartered Accountants in England and Wales

A8: this starts by stating that use of the standard would be inappropriate if entity exhibits the bulleted characteristics but ends with a statement that the bullets are merely indicators of, or proxies for, issues the standard is not designed to address. It is unclear whether the two bullets are to be taken together or individually - 'and' or 'or' needed after the first bullet.

Institute of Chartered Accountants of Scotland

We are supportive of the IAASB's general approach re prohibiting the use of the proposed standard for certain classes of entities, and in addition, describing those qualitative characteristics that would also make the standard inappropriate to use (i.e., collectively describing when the proposed standard is inappropriate for use because the audit would not be considered an audit of an LCE).

The interaction between the bullets in paragraph A8 could be clearer. We believe that the inclusion of a logic condition, "and/or" would improve the clarity of this particular paragraph. Alternatively, the wording in the lead to the bullets could be revised as follows:

"A.8. If an audit engagement is not prohibited from use of the [draft] ISA for LCE as set out in paragraph A.7., it would be inappropriate for an audit of the financial statements of the entity to be undertaken using the [draft] ISA for LCE if the entity exhibits either [or both] of the following:.."

In paragraph A9, there is a risk that the wording implies that other relevant matters do not necessarily have to be considered i.e.

“This list is not exhaustive and other relevant matters may also need to be considered.”

We would suggest revising the wording to either: “This list is not exhaustive and, where applicable, other relevant matters would may also need to be considered.”

Or “This list is not exhaustive, and any other relevant matters would may also need to be considered.”

Korean Institute of Certified Public Accountants

Paragraphs 26, 133, 155 of Explanatory Memorandum prescribes that “while the presence of one ‘complexity’ characteristic exhibited by an entity does not necessarily exclude the use of ED-ISA for LCE for that entity, it would not be appropriate to continue performing the audit under the proposed standard if the complex matter or circumstance identified has not been contemplated in the design of ED-ISA for LCE”. These paragraphs indicate that ‘any matter not contemplated in the design of ED-ISA for LCE can’t be considered in combination and presence of one such matter would exclude the use of ISA for LCE. However, the ISA for LCE doesn’t clearly describe ‘what are the matters not contemplated in the design of ISA for LCE’. Paragraph A.8 simply describes that “such characteristics are indicators of, proxies for, matters or circumstances for which the ISA for LCE has not been designed to address”. Based on paragraph A.8, the characteristics listed in paragraph A.9 appear to be the indicators of or proxies for ‘the matters or circumstances for which the ISA for LCE has not been designed to address.’ Therefore, what the Explanatory Memorandum implies is that the presence of only one of the characteristics described in paragraph A.9 would exclude the use of ISA for LCE, which conflicts with what is described in the latter part of paragraph A.9.

Thus, we believe that the standard needs to be revised to prevent confusion and make it clearer if the qualitative characteristics are going to be listed in the way they are. In particular, detailed explanation should be added to the ED or supplementary guidance needs to be provided to add clarity about (1) how each matter can be considered in combination, (2) circumstance where the ISA for LCE can be used even in case of the presence of listed characteristics, and (3) matters that can’t be considered in combination or circumstances where matters can’t be considered in combination.

South African Institute of Chartered Accountants (2)

It is unclear whether the list of qualitative characteristics provided in paragraphs A8 and A9 is prohibitory or just indicators of a complex environment. E.g. the following is contained within paragraph A8: “If an audit engagement is not prohibited from use of the [draft] ISA for LCE as set out in paragraph A.7., it would be inappropriate for an audit of the financial statements of the entity to be undertaken using the [draft] ISA for LCE if the entity exhibits the following:...”

Further below in paragraph A8: “These are indicators of, or proxies for, matters or circumstances for which the [draft] ISA for LCE has not been designed to address.”

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3g) Comments on Language\General Language used

3. Regulators and Audit Oversight Authorities

Independent Regulatory Board for Auditors (IRBA)

Although the table below paragraph 28 of the Authority Supplemental Guide is somewhat helpful in providing examples of characteristics that may or may not be associated with an LCE, words like “complex” and “straightforward” are still used and provide the same concerns as with paragraph A9.

As such, the IAASB should consider amending the Qualitative Characteristics section (paragraphs A8-A9) of the proposed standard by clarifying what “complex” and “simple”, among others, mean or by using different ways to describe how the Qualitative Characteristics will influence the auditor’s decision as to whether an entity is an LCE.

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 using the proposed standard as set out in paragraph A7.

The Qualitative Characteristics set out in paragraph A9 of the proposed standard – which include: (i) business activities; (ii) organizational structure; (iii) ownership; (iv) oversight; and (v) regulation – are effective indicators against which to measure whether an entity is an LCE or not.

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 will lead to the inconsistent and inappropriate use of the proposed standard among audit firms, and even within audit firms. 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; therefore, a higher level of prescription is more desirable.

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Clarify language in the Authority that is open to interpretation. The lead-in language used in paragraph A.9 may suggest that any one complexity would make the standard inappropriate for the circumstances. We suggest the IAASB consider the following revision to address the perceived inconsistency between the highlighted words:

In accordance with paragraph A.8., the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics may be indicators that the [draft] ISA for LCE is inappropriate for the audit of the financial statements of an entity:

...

The list is not exhaustive and other relevant matters may also need to be considered. Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity.

Finally, practitioners may interpret language in paragraph A.9 such as “high degree” and “significant” differently. This may result in a wide range of interpretations and conclusions. We suggest that the IAASB either revisit this language or provide more guidance and examples to demonstrate what is meant by the terms.

New Zealand Auditing and Assurance Standards Board

Both the proposed standard and the supplemental guidance refer to quantifying adjectives of “few”, “multiple” and “many” (e.g., few employees vs many employees, few levels of management vs multiple levels of management, few products vs many products etc.). These may prove difficult to apply in practice. For example, when do few employees become many? What determines when there are “few” suppliers and when they become “many”? We recommend that the IAASB include more guidance or provide more clarity on how quantitative measures translate into the qualitative judgement that an entity is “less complex”, having regard also to other factors. This could either be suggesting a number range to define these terms and a consideration for firms to further define these when setting the firm’s policies and procedures in the scoping and use of the proposed standard.

5. Accounting Firms

BDO International

As drafted, the ‘qualitative characteristics’ paragraphs effectively state that an entity is not a ‘less complex entity’ if it exhibits complexity. (A.8) This does not help an auditor (or regulator) form a justifiable professional judgment about whether an entity was in scope of the standard or not. A.9 tries to go into more detail, but again defines a less complex entity by what it is not. For example, if an organisational structure is ‘not simple’, it is deemed ‘complex’.

In relation to qualitative characteristics, defining the qualitative traits of less complex entities as being ‘those that do not show complexity’ (a paraphrase of paragraph A.9), does not assist with forming a professional judgment around whether an entity is in scope of the standard or not.

ETY sas

Authority – Qualitative Characteristics

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.

Although the table below paragraph 28 of the Authority Supplemental Guide is somewhat helpful in providing examples of characteristics that may or may not be associated with an LCE, words like “complex” and “straightforward” are still used and provide the same concerns as with paragraph A9.

As such, we believe that the IAASB should consider amending the Qualitative Characteristics section (paragraphs A8-A9) of the proposed standard by clarifying what “complex”, “simple”, etc. means or using different ways to describe how the Qualitative Characteristics will influence the auditor’s decision as to whether an entity is an LCE.

Famme & Co. Professional Corporation

We anticipate these would be challenging to put into practice. We find the use of the terms “topics” and “themes” at paragraph 67 to be particularly outside of the usual terminology and rather vague.

7. Professional Accountancy and Other Professional Organizations

Chartered Accountants Ireland

Paragraph A.9. sets out characteristics which if exhibited by an entity preclude the use of the standard. However, the characteristics are set out in a sweeping manner which will exclude many non-complex entities and the characteristics lack a link to resulting accounting complexity. For example, is a retail point of sales system in a retail entity an example of a highly integrated IT application.

There are areas of the Authority of the standard that are not clear, in particular the Authority of the standard when discussing qualitative characteristics uses very subjective terms rather than objective factors which can be assessed consistently. For example, it is not clear what is meant by “higher degree of regulation”, “emerging markets” or “entities in the development stage”. A typical start-up entity which is not complex would appear to be excluded by the term “entities in the development stage”. Further, the paragraph A.9. sets out characteristics which have a high degree of subjectivity and are therefore not capable of consistent interpretation and application. For example, “Ownership or oversight structures are complex”, “Transactions are complex...” and “...IT systems are complex...” may be subject to different interpretation. To achieve consistent application of the standard, the standard needs to set out the factors that are present when

complexity is present in an entity. In our view, one of the key factors is that the entity's structure, operations, or transactions result in complex accounting in the financial statements such as the need recognise impairment provisions.

Nordic Federation of Public Accountants

To enhance readability, we suggest adding the word “still” in the intro of A.8: “If an audit engagement is not prohibited from use of the draft ISA for LCE as set out in paragraph A.7., it would still be inappropriate...”.

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

Although the table below paragraph 28 of the Authority Supplemental Guide is somewhat helpful in providing examples of characteristics that may or may not be associated with an LCE, words like “complex” and “straightforward” are still used and provide the same concerns as with paragraph A9.

As such, we believe that the IAASB should consider amending the Qualitative Characteristics section (paragraphs A8-A9) of the proposed standard by clarifying what “complex”, “simple”, etc. means or using different ways to describe how the Qualitative Characteristics will influence the auditor's decision as to whether an entity is an LCE.

However, as drafted, these Qualitative Characteristic 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.

Pan-African Federation of Accountants (PAFA)

though the table below paragraph 28 of the Authority Supplemental Guide is somewhat helpful in providing examples of characteristics that may or may not be associated with an LCE, words like “complex” and “straightforward” are still used and provide the same concerns as with paragraph A9.

As such, we believe that the IAASB should consider amending the Qualitative Characteristics section (paragraphs A8-A9) of the proposed standard by clarifying what “complex”, “simple”, etc. means or using different ways to describe how the Qualitative Characteristics will influence the auditor's decision as to whether an entity is an LCE.

However, as drafted, these Qualitative Characteristic 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.

Saudi organization for Chartered and Professional Accountants

Taking into consideration what was introduced in points (a) and (b), we found the excessive emphasis on prohibiting or limiting the use of the standard may have unintended consequences on auditors' willingness to apply the standard. Therefore, since we believe that this proposed standard provides clear, direct and

understandable guidelines which can help specifically SMPs who mostly provide their services to LCEs, we propose amending the discouraging tone of voice introduced in the ED-ISA for LCEs with a more objective approach (restricting the standard's authority approaches to one approach "qualitative characteristics") which can maintain the core requirements while securing the applicability of the standard.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3g) Comments on Language\Inconsistency in A9

3. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies

Characteristics of "less complex entities"

There is an inconsistency in paragraph A9. The first line of this paragraph states that the ISA for LCE is inappropriate for the audit if an entity exhibits "one or more" of the characteristics listed in this paragraph. However, the wording beneath the bullet points seems to contradict this as it states that "The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity.' It is our view that the standard should not be used where one or more of the characteristics listed is present.

Independent Regulatory Board for Auditors (IRBA)

Paragraph A.9 of the proposed standard states the following:

"In accordance with paragraph A.8., the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics:

The entity's business activities, business model or the industry in which the entity operates results in pervasive risks that increase the complexity of the audit, such as when the entity operates in new or emerging markets, or entities in the development stage.

....

This list is not exhaustive and other relevant matters may also need to be considered. Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination."

The first paragraph states that the use of the proposed standard is inappropriate if the entity exhibits one or more characteristics. However, the closing paragraph of this section contradicts this. We suggest that the first paragraph be amended to read as "may be inappropriate ...".

Further, refer to our comments under General and responses to questions 1(a) and 3(a).

Irish Auditing and Accounting Supervisory Authority

There is an inconsistency in paragraph A9. The first line states that the ISA for LCE is inappropriate for an audit if an entity exhibits "one or more" of the characteristics listed in paragraph A9. However, the wording beneath the bullet points seems to contradict this as it states that "the presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity.' It is our view that the standard should not be used where one or more of the characteristics listed is present.

4. National Auditing Standard Setters

Hong Kong Institute of Certified Public Accountants

In addition, we would suggest the IAASB to re-consider the drafting of the following sentences in paragraph A.9. which seem contradictory and confusing:

... the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics

...The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity

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

With respect to the qualitative characteristics, we note our comments to 3 (c) above on the clarity of paragraph A.9 and the need to deal with circumstances not covered by the LCE standard. We also believe that clarification is required that the existence of a qualitative characteristic may not give rise to complexity on its own, but that the aggregate impact of characteristics needs to be considered by the auditor when considering the appropriateness of using the LCE standard.

Public Accountants and Auditors Board Zimbabwe

Other bullet points could just be secondary indicators

The standards also seems self contradictory when it says para A9 “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity.” It seem that this para is proposing and disqualifying at the same time. We think if any of the following is present, then the standard can not be used :

The entity’s operations are subject to a higher degree of regulation or to significant regulatory oversight, such as being subject to prudential regulations.

Transactions are complex or the information system and related processes relevant to the entity’s financial statements are complex such that the data collection and processing involves complex accounting or calculations.

The entity’s IT environment or IT systems are complex, such as when the IT environment and processes involve highly-customized or highly-integrated IT applications, with internal resources or external service providers that have software development and IT environment maintenance skills to support the IT environment and processes.

5. Accounting Firms

BDO International

Some people have interpreted paragraph A.9 very strictly; their understanding is that as soon as one qualitative characteristic exists, the LCE standard is inappropriate. Others have interpreted paragraph A.9 less stringently because of the last three sentences in paragraph A.9 which seem to allow professional judgment in determining if the qualitative characteristics preclude use of the LCE standard. For consistency of implementation in practice, this inconsistency in paragraph A.9 needs to be resolved.

Deloitte Touche Tohmatsu Limited

In addition, because of inconsistencies within the Authority, it is not clear whether having a single “qualitative characteristic that limits use” would prevent application of the proposed standard– see excerpts from paragraph A9 of the proposed standard below, with emphasis added:

“...the [draft] ISA for LCE is inappropriate for the audit of the financial statement if an entity exhibits one or more of the following characteristics”

“Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination.”

KPMG IFRG Limited

We also highlight the following internal inconsistency within paragraph A9:

Paragraph A.9 of the proposed standard states the following:

“In accordance with paragraph A.8., the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics:

The entity’s business activities, business model or the industry in which the entity operates results in pervasive risks that increase the complexity of the audit, such as when the entity operates in new or emerging markets, or entities in the development stage.

.....

This list is not exhaustive and other relevant matters may also need to be considered. Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination.”

The first paragraph precludes use of the standard if the entity exhibits one or more characteristics, however, the closing paragraph of this section appears to contradict this. We consider that the IAASB needs to address this inconsistency.

Mazars

A9 (page 66/170) states “... LCE is inappropriate for the audit of the financial statement if an entity exhibits one or more of the following characteristics”. In the last paragraph in A9, it is stated “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity. Notwithstanding that professional judgment is used in determining whether the [draft] standard is appropriate to use, 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.”

Those sentences seem to contradict each other and might confuse the auditors regarding the applicability of the standard. So we would recommend the change.

Nexia Smith and Williamson

We find the drafting of paragraph A.9 confusing, in that it starts with an explicit prohibition: “the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics” [our emphasis], but goes on to say that “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity” [our emphasis]. This appears contradictory: either one characteristic is sufficient for exclusion or it is not. We agree that one characteristic may not be sufficient on its own to warrant exclusion, and therefore the first part of the paragraph needs to be amended to refer more generally to factors to consider.

Price Bailey LLP

In A9, at the 7th bullet point it refers to “complex methods” with accounting estimates. There could be a number of different interpretations of the types of accounting estimates which would meet that definition, as different firms / audit engagement partners may classify “complex methods” differently. Something that may be seen as complex to one audit partner may seem less complex to someone else who specialises in a particular area.

Paragraph A9 also starts by explicitly stating that ISA for LCE is inappropriate if an entity exhibits one or more of the characteristics listed, but ends by saying that each of these characteristics may on its own not be sufficient to determine whether ISA for LCE is appropriate or not, and also that the presence of one characteristic exhibited by an entity does not necessarily exclude the use of ISA for LCE.

PriceWaterhouseCoopers

We also question whether there is an inherent contradiction within paragraph A9. The paragraph commences by stating “...the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics” but then within the hanging paragraph states “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances...”.

7. Professional Accountancy and Other Professional Organizations

Association of Practising Accountants

As noted above the qualitative characteristics are not clear enough and therefore could lead to challenge from regulators.

Audit clients could see this as a way of reducing audit costs and therefore may push to use this standard when it may not be appropriate. Its intended scope needs to be made very clear so they auditors and their clients can understand when it can and cannot be used. Key areas as noted above is around the accounting estimates.

Paragraph A9 also starts by explicitly stating that the ISA for LCE is inappropriate if an entity exhibits one or more of the characteristics listed, but ends by saying that each of these characteristics may on its own not be sufficient to determine whether ISA for LCE is appropriate or not, and also that the presence of one characteristic exhibited by an entity does not necessarily exclude the use of ISA for LCE for that entity.

Institute for the Accountancy Profession in Sweden (FAR)

In A9 it is stated that "... LCE is inappropriate for the audit of the financial statement if an entity exhibits one or more of the following characteristics". In the last paragraph in A9, it is stated "Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity. Notwithstanding that professional judgment is used in determining whether the [draft] standard is appropriate to use, 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."

In our view these two quotes are contradicting and might confuse the auditors in assessing the applicability in using the standard. The wording in the first paragraph of A9 should be changed to better link to the last paragraph of A9.

Institute of Chartered Accountants in England and Wales

A9: explicitly states that use of the standard is inappropriate if an entity exhibits one or more of the characteristics listed but ends by saying that each of these characteristics may on its own be insufficient to determine whether the ISA is appropriate, and that the presence of one characteristic exhibited by an entity does not necessarily exclude the use of the standard. This is a contradiction and a non-sequitur. We agree that the presence of one characteristic exhibited by an entity should not necessarily exclude the use of the standard and the first part of the paragraph should be amended accordingly. It might instead state that the standard is inappropriate for entities 'displaying some or all the characteristics listed'.

Institute of Chartered Accountants of Scotland

Additionally, there appears to be a contradiction in the logic which has been applied in paragraph A9. At the beginning of this paragraph, it states:

"In accordance with paragraph A.8., the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics:..."

At the final part of A9, it then states: "Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity."

We believe that this needs to be clarified as to whether the presence of one of the qualitative characteristics is sufficient of itself to prohibit use of the proposed ISA for LCE.

Korean Institute of Certified Public Accountants

First part of paragraph A.9 of Explanatory Memorandum prescribes "the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics", whereas the latter part of the same paragraph explains "the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity. There is inconsistency between the first part and latter part of the same paragraph.

Furthermore, there is lack of clarity about how each matter can be considered in combination and about when the ISA for LCE can be used for an entity even though the entity exhibits one of the described characteristics.

Paragraphs 26, 133, 155 of Explanatory Memorandum prescribes that “while the presence of one ‘complexity’ characteristic exhibited by an entity does not necessarily exclude the use of ED-ISA for LCE for that entity, it would not be appropriate to continue performing the audit under the proposed standard if the complex matter or circumstance identified has not been contemplated in the design of ED-ISA for LCE”. These paragraphs indicate that ‘any matter not contemplated in the design of ED-ISA for LCE can’t be considered in combination and presence of one such matter would exclude the use of ISA for LCE. However, the ISA for LCE doesn’t clearly describe ‘what are the matters not contemplated in the design of ISA for LCE’. Paragraph A.8 simply describes that “such characteristics are indicators of, proxies for, matters or circumstances for which the ISA for LCE has not been designed to address”. Based on paragraph A.8, the characteristics listed in paragraph A.9 appear to be the indicators of or proxies for ‘the matters or circumstances for which the ISA for LCE has not been designed to address.’ Therefore, what the Explanatory Memorandum implies is that the presence of only one of the characteristics described in paragraph A.9 would exclude the use of ISA for LCE, which conflicts with what is described in the latter part of paragraph A.9.

Thus, we believe that the standard needs to be revised to prevent confusion and make it clearer if the qualitative characteristics are going to be listed in the way they are. In particular, detailed explanation should be added to the ED or supplementary guidance needs to be provided to add clarity about (1) how each matter can be considered in combination, (2) circumstance where the ISA for LCE can be used even in case of the presence of listed characteristics, and (3) matters that can’t be considered in combination or circumstances where matters can’t be considered in combination.

Nordic Federation of Public Accountants

Paragraph A.9. includes two statements that we believe are contradictory and might confuse the auditors in assessing the applicability of the standard. Firstly, it states that “... LCE is inappropriate for the audit of the financial statement if an entity exhibits one or more of the following characteristics”. In the last paragraph in A.9., it is stated “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity. Notwithstanding that professional judgment is used in determining whether the [draft] standard is appropriate to use, 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.” In our view the wording in the first paragraph of A.9. should be changed to correspond with the message in the last paragraph of A.9.

South African Institute of Chartered Accountants (2)

A similar contradiction has also been identified in paragraph A9:

“In accordance with paragraph A.8., the [draft] ISA for LCE is inappropriate for the audit of the financial statements if an entity exhibits one or more of the following characteristics:”

Further below A9: “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination.”

9. Individuals and Others

ASK KSA Consulting Inc.

The first bullet of A.9 states that if the entity’s business activities result in pervasive risks that increase the complexity of the audit then the standard may not be used. However, as the introduction is written, it states that the standard is inappropriate if an entity exhibits one or more of the listed characteristics. Is that to suggest if that if any of the characteristics are met, the standard cannot be used. If more than one characteristic, the question arises as to how many more. Or, if only one, then does that automatically mean the standard cannot be used?

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3h) Examples, Guidance, Training and Tools\Guidance Training and Tools

3. Regulators and Audit Oversight Authorities

Finance Professions Supervisory Centre Indonesia

Further guidance, training and tools would all be necessary implementation supports initially and on an ongoing basis. In particular, Professional Engagement Guide checklists adapted to the proposed standard would be necessary as a clarity to where the standard fits within an assurance hierarchy.

4. National Auditing Standard Setters

Hong Kong Institute of Certified Public Accountants

We note that the IAASB acknowledges auditors' practical difficulty to assess the use of the proposed standard through qualitative characteristics in paragraph A.9. To address stakeholders' concern, we suggest the IAASB to develop additional guidance or examples on the use of the proposed standard in case of conflicting facts and circumstances exhibited by an entity.

7. Professional Accountancy and Other Professional Organizations

Wirtschaftsprüferkammer (WPK)

The concept of qualitative characteristics in the Authority is basically convincing. However, without further support and guidance we see the risk of inconsistent application across different jurisdictions, audit firms or even audit teams, as the assessment of whether a criterion is met may be interpreted differently. Accordingly, we recommend that additional guidance should be provided, especially regarding the entity's business activities, business model or the industry in which the entity operates.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3h) Examples, Guidance, Training and Tools\Need further examples

3. Regulators and Audit Oversight Authorities

Botswana Accountancy Oversight Authority

The Authority could give examples of applicable qualitative characteristics to enhance the definition of 'qualitative'.

4. National Auditing Standard Setters

New Zealand Auditing and Assurance Standards Board

In principle, the NZAuASB agrees with the proposed limitations relating to use of ED-ISA for LCE established by the QCs. However, the NZAuASB is of the view that the ED does not provide adequate application material for how auditors are to consider areas where an entity may exhibit characteristics that would make it inappropriate to use the proposed standard to audit the entity.

Overall, we are concerned at the potential risk that a lack of clarity on the QCs would result in inconsistent application of the proposed standard and undermine its credibility.

The NZAuASB recommends that the proposed standard provide further clarity on the characteristics that auditors would need to consider as QCs as identified below. The standard should either define blanket QCs that would apply to all areas or define QCs for each area (e.g., for structure, the degree of separation between owner and management, the degree of separation between TCWG of the entity and day to day operations, etc.). It may also be helpful to consider including additional case studies of considerations where there are various QCs to consider with some complex and non-complex characteristics in determining if an entity is a LCE.

7. Professional Accountancy and Other Professional Organizations

Finnish Association of Authorised Public Accountants

What one considers complex is not complex to the other (e.g. Black & Scholes model, cash flow forecasts, goodwill or POC). Therefore, we think that it is useful to give as many practical examples as possible in the EEM or Authority Supplemental Guide. The examples should include not only the most obvious cases but also those in the “grey area”. National guidance is needed so that typical entities and national characteristics as well as laws and regulations can be taken into account. National accounting standards may not include as many complex (or even non-complex) accounting estimates or fair value calculations as IFRS, and this should have an effect on the consideration of complexity at national level.

Institute of Chartered Accountants in England and Wales

The IAASB should consider developing contrasting examples of complex and non-complex estimates, covering, for example, the valuation of share options using a recognised model, the valuation of defined benefit pension schemes, and impairment reviews using discounted cash flows

Korean Institute of Certified Public Accountants

Adding not only typical examples but also more diverse examples to the supplemental guidance and providing the case studies illustrating how professional judgment is exercised in situations when comprehensive judgement is required

We agree with the overall qualitative characteristics proposed in the ED-ISA for LCE. However, as noted in the answer to Question 3, there are significant concerns that current qualitative characteristics are abstract and hard to judge. Such concerns don't seem to be resolved even by the supplemental guidance. We want the qualitative characteristics to be revised to make them more specific, hence less room for exercising judgment. For example, it may be useful to consider following options.

Malaysian Institute of Certified Public Accountants

As indicated, the definition of “Less Complex Entities” needs to be extremely comprehensive and robust to limit uncertainties whether this standalone ISA can be used. We therefore suggest the IAASB to provide illustrative examples pertaining to the application of this proposed ISA for LCE in determining whether an entity would qualify as an LCE. For example, a situation where a company may have simple structure and simple operations, but has fairly complex IT systems to monitor its operations or uses the services of shared service centre, would such an entity be considered as an LCE.

Perhaps, the IAASB can provide us some real-life examples and the guiding principles the IAASB would apply to decide whether the entity is a LCE would be useful as practical application of this standalone standard.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3i) Clearer Link QCs to Procedures

4. National Auditing Standard Setters

Canadian Auditing and Assurance Standards Board

Explain why each qualitative characteristic is included and how it impacts the practitioner's ability to obtain sufficient appropriate audit evidence. Including such an explanation provides context for the practitioner to use professional judgment in applying the Authority to determine whether it is appropriate to use ED-ISA for LCE. For example, explaining how a high degree of regulation may impact the practitioner's ability to obtain sufficient appropriate audit evidence under the ISA for LCE may help practitioners assess this qualitative characteristic.

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

A further matter requiring clarification relates to circumstances when a matter arises that is not covered by the LCE standard. These circumstances need to be made explicit in the criteria (such as not having any

internal audit as defined in ISA 610). Furthermore, requirements and guidance need to be given as to what auditors need to do when such circumstances not covered do arise, such as when an entity has a single individual as an internal auditor. Even though the LCE standard does not cover internal audit, an auditor should not automatically be unable to apply the LCE standard just because a matter is not covered in that standard. One way of dealing with this issue is to provide additional requirements in a separate section or “conditional modules” for such circumstances.

5. Accounting Firms

KPMG IFRG Limited

Additionally, we note that in scoping out estimates that are subject to a higher degree of estimation uncertainty or when the measurement basis requires complex methods as a proxy for complexity, the IAASB has consequently not included certain requirements from the full-scope ISAs that address such estimates within the LCE ISA, since auditors would be expected to use the full-scope ISAs and not the LCE ISA in this scenario. However, since the IAASB has not specifically identified complexity arising from the matters listed above as potential barriers to entry to the standard and has included applicable requirements from the full-scope ISAs in respect of these areas, we believe this could lead an auditor to conclude that, even where complexity arising from these matters does exist, the LCE ISA is still intended to address these matters, and it is therefore appropriate to apply this standard. We consider this interpretation to be inherently inconsistent with the underlying principles regarding use of this standard.

PriceWaterhouseCoopers

We also recommend that clearer statements be made about what the standard does not address, which if present, would result in the standard not being appropriate for use. This could include:

Using the work of internal auditors

Segmental reporting

Accounting estimates involving higher estimation uncertainty and those that involve modelling i.e., determined using methods other than straightforward arithmetical calculations

Certain enhanced auditor reporting, including Key Audit Matters

9. Individuals and Others

Cristian Munarriz

Regarding qualitative characteristics, I think the analysis should be made overall instead of analysis specific factors on an individual basis. It should be clear that the objective of the “qualitative” analysis is related to the lack of consideration of complexity in the ISA for LCE. Therefore if an engagement is considered to be complex, use of the ISA for LCE would be inefficient because of the need to consider additional guidance to address that complexity in order to meet the objectives of the standard and obtain reasonable assurance. The IAASB should consider including a list of examples of factors which may create complexity and how those factors are not addressed in the ISA for LCE, so the auditor may form his or her conclusion regarding the suitability of the ISA for LCE for the engagement objective. It should be clear that existence of isolated complexity factors does not necessarily mean that use of ISA for LCE is not appropriate. It should be clear that if the auditor has significant doubts about the suitability of the use of ISA for LCE in the engagement circumstances, it is likely that ISA for LCE is not appropriate for the engagement (in other words, it should be relatively clear that the engagement is not complex to use ISA for LCE).

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3k) Public Sector NFP Comments

4. National Auditing Standard Setters

New Zealand Auditing and Assurance Standards Board

We also encourage the IAASB to consider if there are additional QCs or nuances to the QCs for public sector and not-for-profit entities.

7. Professional Accountancy and Other Professional Organizations

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

We encourage the board to consider if there are additional QCs that may be useful for auditors of public sector entities as the indicators of complexity may be different for those entities. We suggest the board undertake further outreach with auditors general and other public sector stakeholders to determine if public sector entities may require an amended set of QC's.

We have heard mixed feedback on the qualitative characteristics and whether they may involve too much judgement. However, we recognise that it is difficult to develop bright lines that are suitable for all jurisdictions and overall, allowing the auditors to exercise professional judgement in relation to qualitative characteristics is a balanced approach. We encourage the board to consider if there are additional QCs that may be useful for auditors of public sector entities as the indicators of complexity may be different for those entities.

International Federation of Accountants' Small and Medium Practices Advisory Groups

We also believe there should be additional clarity for non-governmental organizations (NGOs) and whether they would qualify to use this standard if all other criteria are met. For example, during field testing of the authority of standard in Canada, questions arose about when regulated entities are "subject to a higher degree of regulation". Examples of non-complex, but regulated entities include day cares, law firms or real estate agents holding trust accounts, and small insurance brokers / dealers. We believe that if all regulated entities or entities who have regulated operations are excluded, then the pool of potentially eligible entities is greatly diminished in many jurisdictions.

Section 4B – Authority of the Standard\Question 4 - Do you agree with the proposed limitations relating to the use of ED-ISA for LCE\Question 4(b) - Qualitative characteristics\3) Provided Comments\3z. Other Comments

3. Regulators and Audit Oversight Authorities

Finance Professions Supervisory Centre Indonesia

We believe professional judgment should be permitted to be applied in establishing whether an entity is an LCE and that application is documented in the engagement file.

4. National Auditing Standard Setters

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

A further matter requiring clarification relates to circumstances when a matter arises that is not covered by the LCE standard. These circumstances need to be made explicit in the criteria (such as not having any internal audit as defined in ISA 610). Furthermore, requirements and guidance need to be given as to what auditors need to do when such circumstances not covered do arise, such as when an entity has a single individual as an internal auditor. Even though the LCE standard does not cover internal audit, an auditor should not automatically be unable to apply the LCE standard just because a matter is not covered in that standard. One way of dealing with this issue is to provide additional requirements in a separate section or “conditional modules” for such circumstances.

New Zealand Auditing and Assurance Standards Board

In principle, the NZAuASB agrees with the proposed limitations relating to use of ED-ISA for LCE established by the QCs.

5. Accounting Firms

KPMG IFRG Limited

We are generally supportive of the approach to qualitative characteristics described in the standard, and we agree that these would constitute proxies for complexity and that it would be inappropriate to apply the standard in respect of entities with such characteristics. We also welcome the ability of jurisdictional standard-setters/ regulators to refine scoping decisions for certain sub-classes of entities with these characteristics, or to further establish characteristics that are proxies for complexity applicable in their jurisdictions.

RSM International

With the exception of groups, we agree with the specific prohibitions and qualitative characteristics for applying the ED-ISA for LCE, although the IAASB could clarify whether it expects local jurisdictions to set more clearly defined local limitations.

7. Professional Accountancy and Other Professional Organizations

ASEAN Federation of Accountants

We appreciate the qualitative characteristics provided for the auditors (and users) to apply judgment in assessing the use of this standard. To supplement this, the Board may consider introducing some relevant proxies to complexities, to achieve uniform and consistent application of the standard. Several respondents have mentioned about the benefit of presenting quantitative proxies to assist in making consistent judgment.

Roundtable discussion poll: Close to 70% of our respondents believe that the qualitative characteristics set out appropriately describe a typical LCE.

ASSIREVI

With respect to the more specific aspects, in our view, paragraph A.9 of the Authority (referring to the qualitative characteristic represented by the high degree of uncertainty and complexity of accounting estimates and the subsequent considerations about whether the presence of just one qualitative characteristic excludes the entity from the scope of the proposed standard) is not consistent with paragraph 27 of the Explanatory Memorandum.

This paragraph seems to imply that the proposed standard cannot be used “tout court” when the entity has a complex accounting estimate, as the rules established for this by ISA 540 have not been included in the standard and cannot be used to supplement it. Conversely, paragraph A.9 states that the presence of a complex accounting estimate is just one possible characteristic of “complexity” which does not per se exclude the entity from the scope of the proposed standard as the auditor should evaluate all the entity’s qualitative characteristics, i.e., both those set out in the standard as well as others which may be material. The Authority Supplemental Guide (paragraphs 27 and 28) seems to agree with this approach. This Guide states that if an entity’s financial statements include a caption subject to a complex accounting estimate (and, hence, one of those characteristics with a red “x”), this implies it has a qualitative characteristic not usually associated with an LCE. However, if the entity does not have other qualitative characteristics, it could meet the definition of an LCE and, therefore, the proposed ISA for LCE could be applied. Moreover, if the rules to be applied to audit the complex accounting estimates are not included in the proposed ISA for LCE and this proposed standard (due to its rigidity given the decision to make it a standalone standard, separate to the ISAs) cannot be supplemented with the requirements of ISA 540, it would be logical to conclude that the proposed standard cannot be applied when there are complex accounting estimates. To sum up, in our view, should the impossibility of supplementing the standard, as it currently stands, with other rules in the ISAs (e.g., ISA 540) be confirmed, the qualitative characteristic of complex accounting estimates should be treated separately and not as one of the characteristics set out in paragraph A.9 of the Authority and the table in paragraph 28 of the Authority Supplemental Guide.

The same considerations apply with respect to the use of a service organisation by an entity and the auditor’s need to rely on reports on the operating effectiveness of the controls from the entity providing the services (e.g., “Type 1” and “Type 2” reports) and the rules of ISA 402 on their utilisation.

Belgian Institute of Registered Auditors (IBR-IRE)

The possibility left to the professional to interpret qualitative characteristics is useful. However, a few qualitative characteristics referred to in the proposed ISA for LCE do not as such seem to give rise to complexity. Examples can be the IT system, a complex estimate or a start-up operating in a new market.

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

As per our response to 4(a) we believe that the standard should be available to auditors of less complex groups and that the board should include qualitative characteristics that would allow less complex groups to be scoped in.

Chartered Accountants Ireland

Paragraph A.9. sets out characteristics which if exhibited by an entity preclude the use of the standard. However, the characteristics are set out in a sweeping manner which will exclude many non-complex entities and the characteristics lack a link to resulting accounting complexity. For example, is a retail point of sales system in a retail entity an example of a highly integrated IT application

Finnish Association of Authorised Public Accountants

One qualitative characteristic should not usually prohibit the application of ISA for LCE as stated in paragraph A.9. However, it would be useful to have examples on possible situations or kind of issues which could, on their own, be the reason – if there were any. These cases should, however, be limited.

Institute of Chartered Accountants in England and Wales

The Authority must enable firms and regulators to clearly distinguish between entities that are in and out of scope. Jurisdictions applying the standard must facilitate this by the application of additional criteria, if appropriate.

Polish Chamber of Statutory Auditors (PIBR)

I do not accept. Completely new quality solutions must be introduced, including a statistical survey using a representative method.

Saudi organization for Chartered and Professional Accountants

As noted in the general comment, we could not see the necessity of offering two approaches to help professionals (professional regulators and practitioners) in deciding the eligibility of an entity to be deemed LCE. We believe that offering only certain qualitative characteristics can serve the purpose of enriching the judgment of auditors and satisfying the objectives of the standard while securing the proposed design and structure method of the Standard (the principle-based approach). Nonetheless, there are some straightforward prohibitions of certain classes of entities or not, the overall application of the proposed standard is still substantially restricted to auditors' professional judgment. Thus, we propose that the list of prohibited classes of entities can be rephrased and represented as a part of the qualitative characteristics that the auditors have to take into consideration while assessing the appropriateness of using the ED-ISA for LCEs. For example, A.7(c) can be rephrased and represented in the qualitative characteristics section as "one of the entity's main functions involves one of the following; taking deposits from the public, providing insurance to the public...etc." We believe that this could increase the clarity and understandability of the requirement since auditors do not need to get overwhelmed with the existence of two interrelated approaches. Applying this proposed approach is not expected to impact the authority requirement but instead it offers the advantage of limiting variances and repetition of ideas and increases the clarity and, consequently, the understandability and applicability of the requirement. Additionally, the reliance on only one approach which is the "qualitative characteristics" meets the principle-based nature of the ISA and enhances auditors' current responsibility to appropriately use their professional judgment to assess the appropriateness of applying the proposed standard to an entity. Finally, it should be noted that this approach does not contest the idea that the qualitative characteristics list cannot be exhaustive and auditors still need to apply their judgment to assess all relevant matters, nor it contradicts the strict prohibitions and exclusion of certain classes of entities. That can be highlighted, for instance, using a clear statement indicating that "the existence of only one characteristic included in (a), (b)...etc shall make the application of ED-ISA for LCEs inappropriate". The requirements are still the same, but the way they are presented could be more encouraging.

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

The qualitative characteristics are subject to evaluation and discretion of the auditor to arrive at a conclusion of complexity level of the entity. We believe regulatory oversight and review as well as guidelines to be developed at the firm level would be required to assess and lead to avoid huge discrepancies as to the assessments of different auditor and align professional judgment to the extend possible.

9. Individuals and Others

Dmitrii Romanov

According to the draft standard, less complex organizations are understood as small businesses, such as family firms, cooperatives of real estate owners, and the like. In some jurisdictions for small businesses, laws or national accounting standards may provide for significant concessions to preparing financial statement and accounting. The use of these exemptions by the organization could be included in the ISA for LCO as one of the benchmarks (criteria) that would allow the auditor to draw the correct conclusion that an audit of such an organization can be carried out using ISA for LCO.