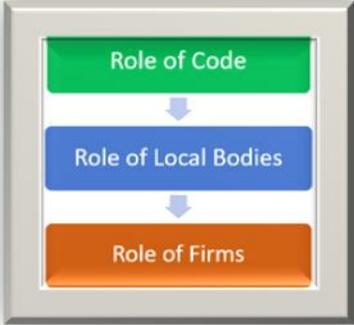


## Definitions of Listed Entity and Public Interest Entity – Issues and Task Force Views

### OVERVIEW

1. At the March 2020 IESBA virtual meeting, the Board considered the Task Force's preliminary views on the PIE project, which included the following two key matters:
    - The overarching objective for defining a class of entities for which the audits require more stringent independence requirements.
    - The Task Force's preferred approach to revising the definition of public interest entity (PIE) which included three key components:
      - a) An expanded high-level list of PIE categories;
      - b) Local bodies, such as regulators and oversight bodies, are expected to refine the list (through more explicit definition or establishment of size criteria); and
      - c) Firms are required to determine if additional entities should be treated as PIEs.
- 
2. Following deliberation of comments from the Board and other stakeholders since March 2020, the Task Force has refined its views and developed proposals for consideration by the Board at its June 2020 meeting that include the following key elements:
    - A revised overarching objective that clarifies there is public interest in the financial condition of certain entities that is relevant to those entities being classified as PIEs.
    - A first-cut draft term as a possible replacement or new definition for the term 'listed entity'.
    - A draft list of PIE categories as well as other possible categories that were considered by the Task Force.
    - Expected role of local bodies and mitigation strategies to address risks that regulators, oversight bodies, national standard setters (NSS) and other relevant bodies do not have the capacity to make the necessary refinements.
    - Role of firms, including a proposal for firms to include in their audit reports whether the client has been treated as a PIE.

#### Matters for IESBA Consideration

The IESBA is asked to provide input to the following:

1. The revised overarching objective set out in paragraphs 400.8 and 400.9 of **Agenda Item 8-B**.

2. Category (a) of the proposed list of PIE categories as a first-cut draft of a possible definition of the term “listed entity,” including whether entities “in the process of being publicly traded” should be included.
3. Category (b) to (f) of the proposed list of PIE categories as well as the Task Force’s consideration of other types of entities.
4. Whether other categories, in particular “custodian,” should be added to the proposed list of PIE categories.
5. Expected role of local bodies and the role of firms under Approach 2.
6. Any other relevant matters.

### **INFORMATION GATHERING ACTIVITIES SINCE MARCH 2020**

3. The Task Force Chair presented the Task Force’s preliminary view at the Forum of Firms’ virtual meeting in March 2020 and the joint IESBA-IAASB NSS virtual meeting in May 2020. The Task Force also sought written input from participants of these meetings with respect to how the term “listed entity” is applied and whether any public markets are scoped out.
4. Members of the Task Force also held informal meetings with a small number of stakeholders including South Africa’s Independent Regulatory Board for Auditors (IRBA), Australia’s Accounting Professional & Ethical Standards Board (APESB), and New Zealand’s External Reporting Board (XRB). All the above NSS have adopted the Code’s International Independence Standards (IIS) and have modified previous material on PIE by including an expanded list of PIE categories and, in the case of IRBA and APESB, a requirement for firms to consider what other entities should be PIEs.
5. Other stakeholders Task Force representatives met included the Zambia Institute of Chartered Accountants (ZICA) and the Financial Stability Board (FSB).
6. The Task Force has also arranged to meet with the International Forum of Independent Audit Regulators’ (IFIAR’s) Standards Coordination Working Group in late May and will report back to the Board at its June 2020 meeting.
7. The Task Force has obtained initial information from IFAC’s Quality and Development Team on the breakdown on the type of responsibility an IFAC member body has to adopt the Code.
8. The IAASB Planning Committee (PC) has briefly discussed the progress of this project. Whilst acknowledging that the Task Force needs to further develop its views on the list of PIE categories and the definition of listed entity, it did not raise any significant concerns. See below for further discussion on coordination with IAASB.
9. In Q2 and Q3 2020, the Task Force will focus on seeking further input from IFAC member bodies and other stakeholders in developing jurisdictions in Asia, Africa and Middle East, and South America. The Task Force also aims to seek views from global and regional stakeholders including, but not limited to, the International Organization of Securities Commissions (IOSCO), the Basel Committee on Banking Supervision (Basel Committee) and Accountancy Europe.

### PIOB Public Interest Issues

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

### **OVERARCHING OBJECTIVE**

11. At the March 2020 virtual meeting, the IESBA generally supported the Task Force's view that it is important, at the outset, to have clarity about the overarching objective for defining a class of entities for which the audits require more stringent independence requirements. The objective can then inform the approach and also provide a clear principle against which any proposals can be tested.
12. At the meeting, the Task Force presented the following proposed overarching objective:

*400.8 Some of the requirements and application material set out in this Part are applicable only to the audit of financial statements in which there is a significant public interest. The purpose of these additional requirements and application material is to enhance confidence in such financial statements through enhancing confidence in the audit of those financial statements*



13. Amongst other matters, IESBA meeting participants provided the following suggestions for refinement for consideration by the Task Force:
  - Whether the proposed objective places too much emphasis on the financial statements per se as opposed to the role of financial statements in relation to confidence in the entity concerned. It was noted that whilst many may regard an entity as a PIE, they may not necessarily look at the financial statements specifically but will take confidence that the financial statements have been properly audited and that independence standards applied to the relevant firms are at a higher level. Similarly, it was queried whether the concept of “public interest in the financial statements” might be perceived as restricted to the interest of investors only.
  - Whether the formulation/framing of the proposed objective might lead to too much focus on those in the financial sector and does not sufficiently cover other entities that are of systemic significance. It was also queried if the Task Force's proposal would capture entities such as public utilities and hospitals in which there is significant public interest.

## Task Force Proposals and Rationale

14. Following review of the comments received, the Task Force has refined the proposed overarching objective as follows (See **Agenda Item 8-B**):

*400.8 Some of the requirements and application material set out in this Part are applicable only to the audit of financial statements of public interest entities, reflecting significant public interest in the financial condition of these entities. The extent of public interest will depend on factors including:*

- *The nature of the business, such as taking on financial obligations to the public as part of an entity's primary business.*
- *Size of the entity.*
- *The importance of the entity to the markets in which it operates.*
- *Number and nature of stakeholders including investors, customers, creditors and employees.*
- *The potential systemic impact on other entities and the economy as a whole in the event of financial failure.*

*400.9 The purpose of these additional requirements and application material for public interest entities is to enhance confidence in their financial statements through enhancing confidence in the audit of those financial statements.*

15. In developing its revised proposed overarching objective, the Task Force:

- Reaffirmed its view that as the material relates to Part 4A, the focus should be on building confidence in the audits of financial statements of PIEs as a result of additional independence requirements.
- Noted that it is not about having a different “level” of independence (as all firms and auditors should be independent when performing an audit engagement) but increasing confidence in that independence.
- Agreed to clarify that the focus on financial statements of PIEs is due to the possible financial impact on stakeholders.
- Is of the view that the revised objective is sufficiently broad to cover any entity that is, from a financial perspective, of systemic significance to the jurisdiction or society in which it operates.
- Agreed to include a non-exhaustive list of factors for determining the level of public interest in the financial condition of entities. This list is largely drawn from the extant paragraph 400.8<sup>1</sup> and is intended to be used by local bodies and firms to determine if entities or categories of entities should be treated as PIEs.
- Notes that the fourth bullet point relates to the direct impact on an entity's stakeholders whilst the fifth bullet point relates to the indirect impact that the entity might have on the overall economic system.

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<sup>1</sup> Section 400, *Applying the Conceptual Framework to Independence for Audit and Review Engagements*

## DEFINITION OF LISTED ENTITY

16. The definition of the term “listed entity” in the Code is identical to that in the IAASB standards and is as follows:

*“An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body”*

17. In considering the project proposal, the IESBA noted that some stakeholders have questioned the meaning of the term “recognized stock exchange” in the definition of “listed entity.”<sup>2</sup> Some have also queried whether that term is intended to be the same as, or broader than, the concept of a “regulated market” in the definition of a PIE in the EU Directive [2006/43/EC](#)<sup>3</sup> (the Audit Directive).

18. As highlighted in the March 2020 issues paper, the Task Force has been considering the following:

- Whether there will be more clarity if terms such as “publicly traded,” “regulated market” or “public market” are used.
- For some “lightly regulated” markets such as over-the-counter markets, where there may well be inherently more risks for investors by design, whether imposing additional auditor independence requirements will meet the overall objective of enhancing confidence in the financial statements.

19. The Task Force has sought input from Forum of Firms (FoF) members with respect to how the term “listed entity” is applied in their networks with respect to independence standards, including whether any securities markets open to the public are scoped out. Responses received (10 in total) indicate the following (See **Agenda Item 8-D**):

- The Code’s definition of “listed entity” is applied even if it includes more markets and exchanges than required by local laws and regulations.
- A few respondents noted that the concept of a “recognized stock exchange” in the Code’s listed entity definition has a broader scope than the concept of a “regulated market” in the EU’s definition of a PIE, and that the Code’s definition covers more exchanges and markets.
- When applying the IESBA definition of “listed entity,” the independence policies of FoF members do not appear to exclude any securities markets that are open to the public. One respondent specifically advised that its network includes over-the-counter markets that are open to the public.

20. The Task Force has sought similar input from the joint IESBA-IAASB NSS meeting participants, with the following key responses received (See **Agenda Item 8-E**):

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<sup>2</sup> See [Summary of Responses](#) (paragraph 32) to the survey of stakeholders for purposes of developing the IESBA Strategy and Work Plan, 2019-2023 (strategy survey).

<sup>3</sup> Article 2.13 of the EU Directive 2006/43/EC, amended by Directive 2014/56/EU, broadly sets out four categories of entity that fall within the meaning of a PIE. Category (a) are “entities governed by the law of a Member State whose transferable securities are admitted to trading on a regulated market of any Member State within the meaning of point 14 of Article 4(1) of Directive 2004/39/EC”

- Whilst a number of the NSS use the term “listed entity” in their independence standards, the term is further defined by legislation in some jurisdictions. For instance, the Brazil Federal Accounting Council noted that “listed entity” in its jurisdiction is defined as entities:
  - a) Registered with Brazil’s security exchange commission (*Comissão de Valores Mobiliários* - CVM). These are companies: (i) that have share, stocks or debt quoted or listed on the Brazilian stock exchange, (*Brasil, Bolsa, Balcão – B 3*), or (ii) that are registered with CVM but do not have shares, stock or debts listed on B 3.
  - b) Registered in a stock exchange abroad or are marketed under the regulations of a recognized stock exchange or other equivalent body.
  - c) Investment funds that have their quotes negotiated in B 3 or in another stock exchange abroad.
- Only one NSS (Germany) has indicated that their definition of “listed entity” as specified in law expressly excludes “secondary regulated markets.” The responses from other NSS participants indicate that the definition of “listed entity” or an equivalent term includes not only the primary markets but also other secondary or alternative markets.
- The US Public Company Accounting Oversight Board (PCAOB) and the US Securities and Exchange Commission (SEC) use the term “issuer,” which includes any public company that is required to file reports with the US SEC or that has filed a registration statement for a public offering of securities. The term also includes other entities that are required by the relevant SEC rules to file financial statements with the SEC.
- The UK Financial Reporting Council (FRC) has adopted the Code’s definition with additional material that provides guidance on how the term should be applied:

*“This includes any company in which the public can trade shares, stock or debt on the open market, such as those listed on the London Stock Exchange (including those admitted to trading on the Alternative Investment Market), and ISDX Markets. **It does not include entities whose quoted or listed shares, stock or debt are in substance not freely transferable or cannot be traded freely by the public or the entity**\* [emphasis added] (e.g. because the listing is a structural requirement for that entity and its shares, stock or debt are not traded, or because the consent of another party is required to trade in the shares, stock or debt...*

*\* For the purpose of reporting breaches to the FRC’s Audit Quality Review, this definition should not be treated as a breach of the International Code of Ethics (IESBA Code).”*

### Task Force Proposals and Rationale

21. As the Task Force continues to develop its thinking in Q3, it is seeking the Board’s initial reaction to category (a) in the proposed list of PIE categories as a first-cut draft of a possible replacement to the term “listed entity” in the extant Code:

*An entity whose shares, stock or debts are publicly traded*

22. The Task Force noted that:

- The above draft term removes the confusion created by the term “recognized stock exchange,” including its relationship with the term “regulated market” in the EU Directive.
- Forum of Firms members have already interpreted the term “recognized stock exchange” to have a broader application than “regulated market” and do not generally exclude entities traded in the less regulated markets (including the “over the counter” type markets).
- NSS participants generally indicated that the application of “listed entity” or equivalent terms such as “issuer” in their jurisdictions includes not only the centralized markets but also the less regulated ones such as over-the-counter type markets.
- In the US, entities listed on the “pink sheets” (a segment of the over-the-counter market in the US) that have met certain thresholds have SEC reporting requirements similar to those for the public companies, and are also subject to certain SEC independence requirements.

#### In the Process of Being Publicly Traded

23. A number of stakeholders have suggested that the PIE definition should expressly include those entities that are in the process of being traded publicly. For instance, such entities are captured in the definition of a “public accountability” entity in the IFRS for SMEs (see opposite).

24. The Task Force considers that this proposal has merit in view of the clear public interest in the financial condition of entities on entering a public market. However, the Task Force has some concern as to whether the phrase “in the process of being traded” might be too subjective – particularly as regards either the time horizon or degree of completion of any process. In addition, the Task Force noted that including entities that were about to join category (a) of the proposed definition might raise questions as to whether the other categories should be similarly expanded (e.g., an entity in the process of applying for a license to carry on deposit-taking business).

25. Another possibility might be to include in the criteria to be considered by a firm in determining whether to treat an entity as a PIE, whether or not before the next audit it was likely that the entity would become a PIE. This would allow some judgement to be exercised by those with the necessary understanding of the position of the entity. Illustrative wording has been included in R400.18 of **Agenda Item 8-B** to show what this might look like.

26. On balance therefore the Task Force has not amended the criteria at this stage, but would welcome the Board’s views on this issue.

***IFRS for SMEs definition of public accountability entity***

***public accountability***

*An entity has public accountability if:*

*(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or*

*(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.*

***publicly traded (debt or equity instruments)***

*Traded, or in process of being issued for trading, in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets).*

## DEFINITION OF PUBLIC INTEREST ENTITY

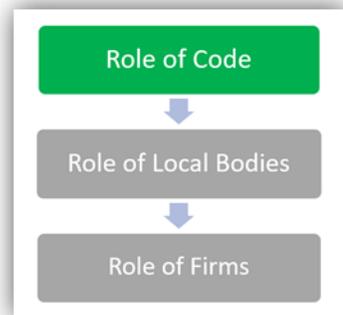
27. The Task Force reached the preliminary view that it would be difficult, if not impossible, to develop a single definition of PIE at a global level that can be consistently applied by all jurisdictions without significant modification and further refinement at a local level. At the March 2020 IESBA virtual meeting, the Task Force presented two approaches that the IESBA could adopt in revising the definition of PIE in the Code:

Approach 1	Approach 2
•A short and narrow list of categories, similar to the current definition of PIE in the Code, to which local regulators and authorities may continue to add	•A longer and more broadly defined list which local regulators and authorities can modify by tightening definitions, setting size criteria and adding or exempting particular types of entities

28. The Task Force also noted that its preference was Approach 2 on the basis that it would be difficult to further refine the current PIE definition under Approach 1, particularly given the principles-based nature of the Code. Approach 1 is also unlikely to meet the expectations of those who would wish the Code's definition to encompass a broader range of PIEs.
29. Under Approach 2, there are three key elements:
- a) An expanded list of categories of entities to be treated as PIEs (Role of Code)
  - b) Expected role of local bodies to refine the list through more explicit definition or establishment of size criteria (Role of local bodies)
  - c) Role of firms to determine if additional entities should be treated as PIEs (Role of firms)
30. The IESBA was generally supportive of the Task force developing its proposals in accordance with Approach 2. A few stakeholders, however, have expressed concern as to whether local bodies such as regulators, oversight bodies and other relevant authorities in some jurisdictions have the capacity to consider and implement the necessary local refinements to the proposed list to ensure the right entities are scoped in within their national contexts. This may lead to the unintended consequence of scoping in entities that should not be treated as PIEs and render the new definition almost impossible to implement in some jurisdictions. This particular concern will be further discussed in the section "Expected Role of Local Bodies."
31. The FoF and NSS participants were also generally supportive of Approach 2 and have not raised any other key concerns with this approach.
32. In light of the support received to date, the Task Force has continued to develop its draft proposals in accordance with Approach 2.

### List of PIE Categories

33. At the March 2020 virtual meeting, the Task Force presented the following initial list of categories based on its review of the various national standards and observations received which led to the initiation of this project:
- An entity whose shares, stock or debts are publicly traded
  - An entity one of whose main functions is to take deposits from the public
  - An entity one of whose main functions is to provide insurance to the public
  - An entity whose function is to provide post-employment benefits
  - An entity that pools money from the public to purchase shares, stock and debts
  - An entity specified as such by law or regulation
34. Following further deliberations, including review of the input received from stakeholders in March and April 2020, the Task Force agreed to present the above list as an initial draft for the Board's further deliberation at the June 2020 virtual meeting.
35. As noted at the March 2020 IESBA virtual meeting, this initial list was based largely on considering those categories already included by a number of countries in their national laws or regulations which set out to define a PIE. In settling on any list, the Task Force believes it is appropriate to include only categories that will (possibly with tighter definitions) be accepted by most countries, and equally, to exclude entities that are only likely to be regarded as necessary by a minority.
36. The Task Force therefore developed the proposed list of categories with the following in mind:
- To include those entities that should be included in this global list because of the nature of their main functions but would be excluded by the local bodies if they are too small (i.e., the entities in these categories are scoped in unless local bodies consider them to be insignificant); and
  - Conversely, not include those entities that would be included by local bodies principally because of the size of the entities (i.e. these entities, such as large private companies, are scoped out unless they are significant enough to be included by local bodies)
37. If the Board agrees with the position set out in paragraphs 35-36, the list should be considered in that light.
38. During the various discussions both at the Board and subsequently with stakeholders, some questions have been raised about the categories originally proposed – both as regards categories that might be excluded and those that might be included. These categories are set out below together with the Task Force's observations. The Board is invited to comment on each category with a view to determining whether any of them should be included as a proposed PIE category or not or if further information is required before making such a determination. If the latter, then the Board is asked to specify what information that is.



### Categories Whose Inclusion was Questioned

39. The only category in the original list that was questioned was category (d) – An entity whose function is to provide post-employment benefits. In this regard, one Board member was concerned that this was drawn too widely and might capture a number of entities inappropriately. This comment was echoed by one of the NSS. Whilst the Task Force appreciates this concern, it still regards this category to be generally appropriate. It would clearly be expected that national regulators would further refine this definition having regard to the nature of post-employment benefits provided and the structure (and potentially size) of the entities concerned.

### Other Possible Categories Considered

#### 40. *Custodians*

- One Task Force member and others including a representative of the FoF and the NSS have raised the question of whether the list should specifically include custodians, although this is not generally a category which has been included to date by national regulators.
- A custodian either of assets or of cash is an entity (often a financial institution) which maintains assets (which may include cash) on behalf of third-party clients. Custodians can take different forms – from those simply providing such services to those that also provide advisory or investment management services. In addition, they may act as sub-custodians for other custodians. Where title to investments is held electronically, a central securities depository (such as the Depository Trust Company or the various Euroclear subsidiaries in the European markets) also in effect acts as the ultimate custodian. Generally such third party assets (including cash) held by a custodian do not feature as part of the custodian's own financial statements, although some operational cash balances may be shown on the balance sheet offset by an equivalent liability to the client.
- The third-party clients on whose behalf the assets are maintained may (as noted above) be other custodians, members of the public (for example, individuals with broker dealer accounts) or mutual funds (generally run by investment managers).
- There is clearly a public interest in ensuring the proper maintenance and integrity of the systems used to control and report on the client assets held by a custodian. In this regard, the role of the auditor of the custodian's financial statements may vary, although at some level there is clearly a need for the financial statement auditor to consider if the custodian is complying with laws and regulations as regards its operations. This can be extended to more direct responsibility for reviewing compliance with those rules, often with separate reporting (public or private) to regulators. Whilst such reporting may be performed by the statutory auditor of the financial statements this is not necessarily a requirement. In addition, if the custodian's client is itself subject to audit then its auditor will often require the issuance of a controls report (for example under IAASB's ISAE 3402<sup>4</sup>) to support the existence of the client's assets – again often but not necessarily issued by the custodian's financial statement auditor. This can in turn impact what regulatory reports are required – for example, in the US a qualified custodian is subject to a surprise examination of its custody systems by an auditor (which does not need to

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<sup>4</sup> International Standard on Assurance Engagement (ISAE) 3402, *Assurance Reports on Controls at a Service Organization*

be the same firm as performs the audit of the financial statements), unless the investments are held on behalf of a pooled investment vehicle which itself has an appropriate audit.

- The Task Force itself has not reached a consensus on including such entities in a definition of a PIE for Part 4A of the Code and would welcome the Board's input on this question, including whether reporting on the safe custody of assets might fit better in the context of Part 4B.

#### 41. *Charities*

- Charities cover a broad range of sectors such as social and welfare, health, arts and religion. In this regard, it may be argued that the level of public interest in these entities may vary depending on the nature of their operations and services. For instance, the public interest in the financial conditions of a welfare organization on which its beneficiaries are significantly dependent may be different to that of a local sporting club that is also registered as a charity.
- Charities also vary in size – in terms of donations, the number and type of donors and beneficiaries, as well as number of employees. For instance, whilst the Bill and Melinda Gates Foundation is one of the largest private foundations in the world, it only has a small number of donors and distributes its money to grantees (often other charities) instead of directly for the benefit of members of the public. This may be contrasted with the Red Cross which runs programs that directly benefit those at risk, and receives donations from a broad spectrum of society.
- The Task Force noted that Singapore's [ISCA Code](#) includes large charities and large institutions of a public character as PIEs if they meet certain size thresholds as defined by laws and regulations. Similarly, New Zealand's [XRB Code](#) also includes not-for-profit entities of a certain size as PIEs. Whilst charity is not listed as a category of PIE in its local Code, the APESB has recently published a [draft independence Guide](#) that includes an illustrative example of a large charity as an entity that firms might determine to treat as a PIE.
- The Task Force is, however, of the view that the public interest in the financial condition of a charity will vary considerably depending on factors such as size, nature of services and number of stakeholders. Accordingly, it is not appropriate to include charities as a separate category of PIE in a global code.

#### 42. *Public Utility Entities*

- A public utility entity provides essential services to the public such as electricity, gas, water and postal services.
- Whilst there may be significant public interest in the continuing operations of a public utility entity because of the essential nature of the services it provides, the level of public interest in the financial condition of such entity will depend on a number of factors. Such factors may include the source of funding and whether the provision of services can be readily replaced by other service providers.
- For instance, whilst there is a high level of public interest in the provision of gas services in a metropolitan area, the level of public interest in the financial condition of a privately owned public utility entity that distributes gas in that area may not be high if its services can be easily picked up by its competitors.

- In addition, as one IESBA member pointed out at the March 2020 virtual meeting, it is also unclear which aspect in the provision of an essential service would render a public utility entity a PIE – the generation, transmission or distribution of a service, all of which may be undertaken by separate entities.
- Accordingly, the Task Force is of the view that public utility entities should not be included as a separate PIE category.

43. *Public Sector Entities*

- Similar to the rationale relating to public utility entities, the Task Force is of the view that whilst there may be significant public interest in the continuing operations of a public sector entity, the level of public interest in the financial condition of such entity will depend on a number of factors. In addition, many public sector entities are audited by other arms of government rather than by professional accountants.
- Accordingly, the Task Force is of the view that public sector entities should not be included as a separate PIE category.

44. *Large Private Companies*

- The Task Force is of the view that what is “large” will vary from jurisdiction to jurisdiction and would be impossible to define at a global level. Whether there is sufficient public interest in the financial condition of a particular private company or types of private companies will depend on factors such as those included in the proposed paragraph 400.8 (See **Agenda Item 8-B**).
- The Task Force noted that under the UK FRC’s revised [Ethical Standard](#) as of December 2019, the statutory audit of an entity that meets the definition of “other entity of public interest” (OEPI) is subject to certain independence requirements with respect to the provision of non-audit/additional services. Under the UK FRC’s revised [Glossary of Terms](#), large private companies that meet certain thresholds and criteria are deemed to be OEPIs.
- Similar to approach taken in the UK FRC standard, the inclusion of any private companies or categories of private companies should be considered only at the local level. For instance, some jurisdictions might determine that any private companies that are required to file certain types of financial statements should be added as a category of PIE.
- Accordingly, the Task Force is of the view that large private companies, including any companies that were once public companies, should not be included as a separate PIE category.

45. *Private Equity Funds*

- Private equity funds by nature receive investments from only institutional investors and do not attract funds from the public directly.
- Similar to the rationale for large private companies, the Task Force is of the view that whether there is sufficient public interest in the financial conditions of a private equity or types of private companies will depend on factors such as those included in the proposed paragraph 400.8.

46. *Systemically Significant Entities*

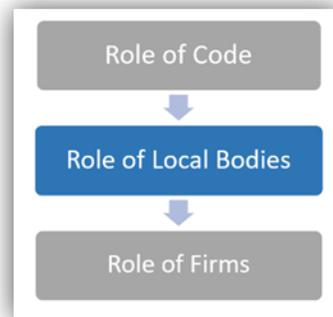
- The Task Force also considered whether, in addition to financial institutions that are systemically important, there are other systemically significant entities that should be included as a PIE category.
- A systemically significant entity is an entity whose potential failure may cause serious harm to other industries and to the economy, or an entity that is “too big to fail.” In this regard, the Task Force chair had a discussion with a representative of the FSB. It was noted that aside from the large banks, it had as yet not been possible to achieve a global consensus on what other types of entities might be of systemic significance, although there had been some consideration of major insurance companies and hedge funds/asset managers.
- The Task Force is therefore of the view that whilst whether an individual entity has a systemic significance should play a part in the criteria used to determine if an entity is a PIE, the term is too subjective and requires too much local context to usefully include it as a separate category.

47. *Public Accountability Entity*

- With regards to the first part of the IFRS’ definition of public accountability entity, this was discussed in paragraph 23 of this paper. With regards to the second part of the definition that relates to an entity holding assets in a fiduciary capacity (as this term is used by the IASB), the Task Force is of the view that these entities are already sufficiently included in the proposed revised categories of PIE.

**Expected Role of Local Bodies**

48. Given the high-level nature of the proposed expanded list, Approach 2 requires local bodies to assess and determine which entities or types of entities should be treated as PIEs for the purposes of additional independence requirements. The Task Force is of the view that local bodies, be it the NSS, regulators, oversight authorities or other relevant bodies, are also best placed to consider the issues, concerns and nuances specific to the local environment and how the financial conditions of certain entities or categories of entities might impact the public interest in their jurisdictions.



49. In following Approach 2, the Task Force is also conscious that any categories it seeks to include will, being principles based, inevitably be quite broad and could therefore scope in entities in which the public interest is not significant. The Task Force therefore believes it is appropriate in these circumstances that the Code should deviate from its normal practice and allow local law or regulation to prevail where the local law or regulation would tighten those broad categories to exclude entities that the Code would otherwise include as PIEs.

50. The Task Force also considered the concerns raised by some IESBA members and other stakeholders that some regulators may not have the requisite capacity, in the sense of capability, knowledge and resource, or the authority to make the necessary assessment and refinements to a list of high-level PIE categories in their local Code. Further, the Task Force recognized that some jurisdictions might simply adopt the Code as is without much refinement, a step which is pivotal to

Approach 2. The Task Force acknowledged that this issue may significantly impact the adoption or implementation of the changes to the definition of PIE developed under Approach 2 by a large number of jurisdictions.

51. The IRBA, APESB and XRB have all adopted the IIS, including the material on PIE, and have further developed a list of PIE categories in their local Code. The Task Force also noted that:
  - All three stakeholders were supportive of the Task Force’s approach as they have developed an expanded list to bring more clarity and consistency amongst firms about how the term “PIE” should be applied.
  - Each of these expanded lists was developed in conjunction with the relevant local industry regulators and authorities given their knowledge and sphere of expertise in the various industries. Whilst the process of developing such a list for local use was time-consuming, the exercise was worthwhile, and they had not received comments from stakeholders that would suggest otherwise.
52. The ZICA, as an IFAC member body, has the authority to adopt the IESBA Code. A representative from ZICA noted that the local Code currently includes banking institutions and insurance companies. The ZICA representative added that ZICA will consider adding other categories of PIE if the IESBA revises the definition of PIE by expanding the list of PIE categories.
53. To better assess the nature and extent of this issue, the Task Force will seek further input from global stakeholders such as IFIAR and IOSCO as well as stakeholders at local levels, particularly those in smaller jurisdictions in Asia, Africa and South America.

Adoption Responsibility Across Jurisdictions

54. The Task Force is also working with IFAC’s Quality and Development (Q&D) Team to gain a better understanding of which body has the authority to adopt the Code in the jurisdictions – noting that in



less developed jurisdictions this could well be the IFAC member bodies.

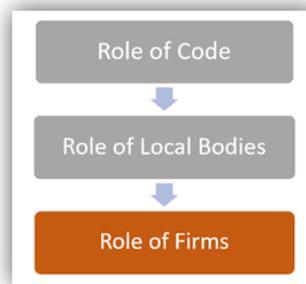
55. IFAC's *International Standards: 2019 Global Status Report* indicates that 17% of professional accountancy organizations (PAOs) have direct responsibility to adopt the Code, 69% have shared responsibility and 14% have no responsibility. This means 86% of PAOs have full or partial responsibility to adopt the Code.
56. The more jurisdictions that are in the first and second categories (i.e., "direct responsibility" and "shared responsibility"), and the more developing the jurisdictions in these two categories, the more likely that the Task Force's mitigation strategy (see section below) will successfully address the risk of regulators not having the necessary capacity to refine the proposed PIE definition.
57. Additional data from the Q&D Team provided to the Task Force also indicate the following:
  - There are about 30 jurisdictions in which the PAOs have direct responsibility, 80 shared responsibility, and 20 no direct responsibility.
  - Approximately one third of the "direct responsibility" jurisdictions are from Africa.
  - The majority of the EU member states and non-EU European jurisdictions are in the "shared responsibility" category. The remaining EU member states are in the "no direct responsibility" category.
  - Whilst jurisdictions in the "no direct responsibility" category will prima facie be the most problematic, it is noted that this category includes EU member states and countries such as Australia and New Zealand where the PIE definition has already been sufficiently articulated. There are about 10 jurisdictions in this category that are smaller or developing jurisdictions, spread across Asia, South America, and Middle East and Africa.

#### Mitigation Strategy

58. Subject to the outcome of discussions with stakeholders, the Task Force has identified the following mitigation strategy to address this issue:
  - The new overarching objective should provide high level guidance.
  - Develop non-authoritative guidance material in addition to the Explanatory Memorandum and the Basis for Conclusions, and conduct outreach to targeted stakeholders with assistance from IFAC, leveraging IFAC's resources and existing networks.
  - Allow for a longer transition period to provide sufficient time for local bodies to engage with stakeholders and develop their list.

#### **Role of Firms**

59. The third component of Approach 2 relates to the role of firms. At the March 2020 IESBA virtual meeting, the Task Force presented its preliminary view:
  - Firms should be required to determine if any additional entities, or certain categories of entities, should be treated as PIEs. The extant material in paragraph 400.8 currently only encourages firms to make such determinations.



- Whilst local bodies can refine the PIE list, firms should only be allowed to determine if additional entities should be treated as PIEs. In making such determination, firms should be reminded to apply the reasonable and informed third party test.
  - The Task Force recognizes that in some instances, an entity and other stakeholders might also request the firm to treat the entity as a PIE. Whilst this should as a principle be generally encouraged, the firm would also need to consider whether such treatment is appropriate taking into account such factors as the entity's corporate governance arrangements, given the various stipulations on communication with those charged with governance (TCWG) of PIEs.
60. The IESBA was generally supportive of the Task Force's preliminary view, with a few IESBA participants querying whether firms need, or are able, to make such determination for all their clients.
61. The FoF and NSS participants also did not raise any concerns with the proposed change.
62. As highlighted in the March 2020 papers, both the APESB and the IRBA have elevated to a requirement the application material in paragraph 400.8 of the IESBA Code that encourages firms to determine whether to treat additional entities, or certain categories of entities, as PIEs.
63. The APESB and IRBA representatives indicated the following in support of the new requirement:
- Both the APESB and IRBA did not receive any major concerns from firms since their revisions became effective in 2013 and 2016 respectively.
  - The new requirement allows inspectors to ask firms how they formed the decision as to whether an entity is a PIE or not, resulting in a greater level of consistency across firms.
  - The IRBA representatives gave the example of higher education institutions in South Africa. They explained that the presence of a university can be a major driver of the economy for a particular town and the public in that area would conclude that it is a PIE. In this regard, they noted that firms are consistently determining to treat the 21 institutions of higher learning in South Africa as PIEs.
64. In light of the above, the Task Force remains of the view that the proposed elevation of application material to a requirement should be retained.

#### Transparency

65. During the March 2020 IESBA virtual meeting, the Task Force pointed out that one effect of its proposals may be increased uncertainty as to whether an entity has been treated as a PIE, particularly if this determination has been made by a firm rather than as established by law or regulation.
66. To address this issue, the Task Force suggested that it will explore with the IAASB the option of adding a requirement in the International Standards on Auditing (ISAs) for audit reports to reference or disclose whether the particular entity was treated as a PIE if it is not otherwise clear from the financial statements themselves. In this regard, early indications from IAASB correspondent members are that the IAASB should not have any major concerns to this proposal.
67. It is anticipated that the IAASB will discuss this matter during its upcoming session on the PIE project. The Task Force will update the Board on the outcome of the IAASB's discussion at the September 2020 IESBA meeting.

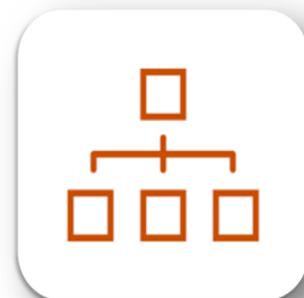
## Other Matters

### SPIE vs PIE

68. At the March 2020 virtual meeting, the Task Force suggested that the term “significant public interest entity” (SPIE) may be more appropriate than the term “PIE” as the latter may give the perception that only PIEs have any level of public interest. The Task Force also noted that “SPIE” also has the benefit of distinguishing that term from the current use of the term “PIE” in the extant Code.
69. A number of IESBA members and CAG representatives expressed their preference to retain the term “PIE” on the basis that it is a well-established term and that the word “significant” in “SPIE” may create another level of judgment.
70. Upon deliberation, the Task Force agreed that, on balance, the term “PIE” should not be replaced by “SPIE” but that the phrase “significant public interest” should be retained in the proposed paragraph 400.8 to denote a higher level of public interest in the financial condition of an entity that requires its audit to be subject to additional independence requirements.

### Related Entity

71. The extant Code contains only one reference of “listed entity” in the IIS that is separate from its treatment as a PIE. This reference, in paragraph R400.20, specifies to which related entities the independence provisions applicable to the audit client should also apply, depending on whether it is a listed entity or not. When an audit client is a listed entity, reference to audit client in the IIS includes all of that entity’s related entities (upstream, downstream and sister entities, as defined).
72. As part of its review of the definitions of PIE and listed entity, the Task Force informed the IESBA and CAG in March 2020 that it will also consider whether extant paragraph R400.20 with respect to related entities (the “related entity provision”) should be updated by changing the reference to listed entity to PIE.
73. The Task Force has previously noted that if all related entities are included in the definition of an audit client when the client is a PIE, there may be practical difficulty in identifying, and obtaining the necessary data of, all related entities for non-listed entities. The Task Force has heard that mapping out the entire organizational chart of a non-listed entity can be challenging in some jurisdictions. Further, clients may not be timely with updating their information on acquisitions or divestures and therefore it may be difficult for auditors to obtain accurate information.
74. One IESBA member also pointed out to the Task Force that, in some circumstances, the expansion to PIE from listed entity within the related entity provision may significantly restrict the choice of auditors for some entities. For example, it was noted that there are countries where the sovereign wealth funds and government provident funds have interest in a multitude of portfolio entities. If all the portfolio entities are related entities and, because of the government link, all other government-linked entities are related entities the auditee will not have much choice of auditors. Without that choice, any firm that takes on the audits will immediately breach the fee dependency threshold. The IESBA member further suggested that if the categories of PIEs are expanded, the IESBA should in fact consider narrowing the related entities definition to downstream controlled entities, possibly only



downstream non-PIE controlled entities because a downstream PIE entity will have its own governance and TCWG. The IESBA member noted that in Asia, it is common for a listed entity to control another listed entity but have different management and board. In such circumstances, the IESBA member suggested that each entity should be given the autonomy.

75. In developing its view, the Task Force will also coordinate with IESBA's Engagement Team – Group Audits Task Force as that Task Force considers the impact on the Code of the proposed changes to the engagement team definition in the IAASB's proposed ISA 220 (Revised)<sup>5</sup> as well as its proposed changes to ISA 600 on group audits. Amongst other matters, the Engagement Team – Group Audits Task Force will consider revisions to the IIS to clarify the application of the IIS in a group audit context, including with respect to independence for non-network component auditors. As such, any proposed changes to how the definition of "related entity" is applied in relation to "audit client" under extant paragraph 400.20 will have implications for the scope of the Engagement Team – Group Audits Task Force's investigation and analysis.
76. The Task Force will provide its views on whether to expand the category of audit clients that include all related entities to PIE for consideration by the IESBA at its September 2020 meeting.

## COORDINATION WITH THE IAASB

77. Coordination with the IAASB is important for this project given the following objectives:
- Establish agreement between the IESBA and IAASB on a common revised definition of the term "listed entity" that would be operable for both Boards' standards.
  - Develop a pathway that would achieve convergence between the concepts underpinning the definition of a PIE in the Code and the description of an entity of significant public interest (ESPI) in the IAASB standards to the greatest extent possible.
78. With the above in mind, the following coordination plan was agreed upon:
- IAASB correspondent members continue to be the first point of contact to provide views at Task Force meetings and to identify relevant issues for report-back to the IAASB Planning Committee (PC).
  - IAASB PC to discuss the project as needed.
  - IAASB to deliberate the relevant issues in a separate session before September 2020.
  - Joint IAASB-IESBA plenary session in Q4 2020.
79. As mentioned above, in May 2020, the IAASB PC briefly discussed the progress of this project including the Task Force's preferred approach. The IAASB PC agreed that to facilitate early feedback to the Task Force, the IAASB should discuss the proposals in a separate virtual meeting in late July 2020.

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<sup>5</sup> Proposed International Standard on Auditing (ISA) 220 (Revised), *Quality Management in an Audit of Financial Statements*

## IAASB Standards and Proposed ISQM 1 and 2<sup>6</sup>

80. The approach that is applied in the IAASB's Standards today is to include the ISAs or the [proposed] ISQMs, in some circumstances as appropriate, certain requirements that are designed to only apply to the firm or the auditor when auditing the financial statements of a listed entity. This is because of the public interest considerations around audit quality related to listed entities. In this context, the only type or category of entity which is accommodated in the requirements of the relevant ISAs separately from other entities is listed entities.
81. In some instances, application material is also added to alert auditors that it may be appropriate to apply a requirement that was designed for an audit of financial statements of a listed entity, to a broader range of entities. Hence, the use of the ESPI concept that recognizes that certain entities other than listed entities might have characteristics that give rise to similar public interest issues as listed entities.

### Listed Entity

82. The definition of the term "listed entity" in IAASB standards is identical to that in the Code. The term is used in IAASB Standards specifically in relation to requirements for:
- Communication of certain matters to TCWG in an audit of financial statements in ISA 260 (Revised), *Communication with Those Charged with Governance*.
  - Reporting for audits of financial statements of listed entities in ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*.
  - Communication of key audit matters in the auditor's report in ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*.
  - Reporting of other information for audits of financial statements of listed entities In ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*.
  - The performance of an engagement quality control review for an audit of financial statements pursuant to International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*. The reference to "listed entity" is retained in the latest draft of proposed ISQM 1 (proposed paragraph 41A(e)).
83. The term "listed entity" is also included in the proposed ISQM 1 as an example of a factor for consideration under the material on scalability when a firm develops a system of quality management (proposed paragraph 13A).

### ESPI

84. The concept an "ESPI" is currently used in IAASB Standards specifically in the application material for ISAs 260 and 700. The description of ESPI in these standards is similar to the factors described

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<sup>6</sup> Proposed International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*; and proposed ISQM 2, *Engagement Quality Reviews*

in paragraph 400.8 of the extant Code for consideration by firms when determining if additional entities should be treated as PIEs.

85. In the ISQM 1 ED, the concept of “ESPI” was proposed as a factor for consideration by firms when determining if an engagement quality review is necessary. However, the IAASB agreed to remove the term from the proposed text in response to comments from respondents that the concept was unclear.

### **Next Steps**

86. As mentioned above, the Task Force is arranging to meet with stakeholders such as IFAC member bodies and regulators, with a focus on developing jurisdictions, in Q2 and Q3. In July, the Task Force anticipates presenting its views and draft proposals at an IAASB virtual session.
87. The Task Force will present its revised proposals to the IESBA and CAG during their respective September 2020 meetings.
88. The Task Force will also continue to monitor its progress in light of the impact of COVID-19 on stakeholders and the availability of resources. It will discuss with the IESBA in September 2020 whether it would be more appropriate to aim for a discussion paper instead of an ED in December 2020.