



The Chairman

IAASB
International Auditing and Assurance Standards Board
529 5th Avenue
New York, NY 10017
USA

28 January 2022

Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)

Dear Sirs:

Assirevi is the association of the Italian audit firms. Its member firms represent the vast majority of the audit firms licensed to audit companies listed on the Italian stock exchange and other public interest entities in Italy, under the supervision of CONSOB (*Commissione Nazionale per le Società e la Borsa*).

Assirevi promotes technical research in the field of auditing and accounting and publishes technical guidelines for the benefit of its members. It collaborates with CONSOB, the Italian accounting profession and other bodies in developing auditing and accounting standards.

Assirevi is pleased to submit its comments on the Exposure Draft "*Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)*" issued by IAASB in July 2021.

Our detailed comments are set out in the attached document.

Should you wish to discuss our comments please do not hesitate to contact us.

Yours faithfully,

A handwritten signature in black ink, appearing to read "Gianmario Crescentino".

Gianmario Crescentino
Chairman

(Enclosure)

COMMENTS ON THE IAASB EXPOSURE DRAFT

Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE) (July 2021)

Section 4A – Overarching Positioning of ED-ISA for LCE

1. Views are sought on:

- (a) **The standalone nature of the proposed standard, including detailing any areas of concern in applying the proposed standard, or possible obstacles that may impair this approach?**

As we commented in the Discussion Paper “Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the ISAs” issued by the IAASB in April 2019 (the “DP”), we believe that while, in theory, the standalone nature of the proposed standard, specifically applicable to audits of less complex entities (LCEs), is consistent with the requirements and pre-set objectives, its practical application could have negative consequences that would outweigh the potential benefits. In particular and given the considerable importance of the LCEs to the economic and social context (especially in Italy), we believe that the proposed standard may generate confusion for the stakeholders about the nature of an audit conducted in accordance with ED-ISA for LCE. This could widen the expectation gap or even create the perception that there are two different audit categories:

- the audit of LCEs for which just one standard is sufficient (“...with no intended need to directly reference back to the requirements or application material in the ISAs in its application...”¹) and, hence, without having to reference the entire set of ISAs); and
- the audit of more complex entities to be conducted in accordance with an articulated and complete set of standards.

This different approach to the audit of LCEs, which could diminish stakeholders’ confidence due to the standalone nature of the proposed standard, would be seen in the auditor’s report as it cannot (correctly) refer to the complete set of ISAs.

This could decrease the reliance placed on the financial statements of the LCEs and the auditor’s report by their potential users as well as reduce the overall degree of confidence in the audit profession.

Although the enormous project carried out by the IAASB to develop the proposed standard based on the nature and characteristics typical of the LCEs is much appreciated, we have identified some important critical issues and application difficulties:

- while obviously keeping faith with the general objectives of the ISAs, the proposed standard does not seem to have been simplified enough to justify

¹ Paragraph 26 of the Explanatory Memorandum.

its standalone nature compared to the complete set of ISAs. In fact, some requirements, the application of which is tied to and/or dependent on the existence or not of certain events and circumstances, have been eliminated or, in some cases, rewritten, and, therefore, they would presumably not be relevant to the audit of an LCE². On the other hand, for example, the risk assessment process which underpins the entire audit process, as set out in the proposed standard, has maintained nearly all the rules envisaged by ISA 315R, including the need to assess inherent risk (both with respect to the likelihood of occurrence and the magnitude of a misstatement) and control risk separately. The requirement to measure all components of the internal control system, as established by this proposed standard, continues to hold true, including the entity's risk assessment process and the monitoring of controls, which are often difficult to assess or are not suitably structured in LCEs. Indeed, in our view, the analysis and evaluation of internal controls is the main challenge in the audit of an LCE: as a matter of fact, the LCE's structure normally implies a less sophisticated internal control system as well as, often, an insufficient segregation of duties.

- As explained in paragraphs 26 and 27 of the Explanatory Memorandum, the proposed standard's standalone nature and the impossibility to reference back to the ISAs makes it very rigid, requiring the auditor to assess and decide - before conducting the audit - whether the standard is appropriate for use based on the nature and characteristics of the entity. Moreover, if certain circumstances arise during the audit engagement, the auditor has to decide whether to transition to the ISAs, which could be a complex and onerous process. Therefore, the auditor could encounter complications with the definitions contained in the proposed standard, as given the difficulty in defining the characteristics of the LCEs with sufficient precision and/or detail, the IAASB has decided to define the characteristics of entities that do not qualify as LCEs and for which the use of the proposed standard is prohibited or can only be applied with limitations.
- The proposed standard's structure, organised by considering the audit work flow rather than by topic, like the ISAs, means it is easier to understand and apply, especially by auditors that do not have in-depth and consolidated knowledge and experience in applying the ISAs and the related objectives and general requirements. Conversely, auditors that have always applied the ISAs may continue to refer to them rather than to the proposed standard using the Mapping Documents to intercept inapplicable requirements. Again in this case, there is a risk that the quality of the audit may vary depending on the nature and characteristics of the audited entity.

In our view, these critical issues could hinder achievement of the objective of conducting an audit effectively for the LCEs. We believe that this objective could be achieved through the greater scalability and proportionality of the ISAs (despite their greater length, complexity and structure). This would allow the consistent application of the ISAs, including through practical guidance, to ensure a quality audit of all entities regardless of their size or complexity.

² See paragraphs 102 and 106 of the Explanatory Memorandum.

(b) The title of the proposed standard

We believe the title of the proposed standard is consistent and appropriate given that it is a standalone, separate standard that is still, however, an international standard issued by the IAASB.

(c) Any other matters related to ED-ISA for LCE as discussed in this section (Section 4A).

Nothing to report.

2. Do you agree with the proposed conforming amendments to the IAASB Preface (see paragraphs 39-40)? If not, why not, and what further changes may be needed?

We agree.

Section 4B – Authority of the Standard

3. Views are sought on the Authority (or scope) of ED-ISA for LCE (Part A of the proposed standard). In particular:

- (a) Is the Authority as presented implementable? If not, why not?**
- (b) Are there unintended consequences that could arise that the IAASB has not yet considered?**
- (c) Are there specific areas within the Authority that are not clear?**
- (d) Will the Authority, as set out, achieve the intended objective of appropriately informing stakeholders about the scoping of the proposed standard?**
- (e) Is the proposed role of legislative or regulatory authorities or relevant local bodies with standard setting authority in individual jurisdictions clear and appropriate?**

In light of the strong interconnection between the questions above, we believe it is appropriate to address them jointly.

As set out in point 1(a), we believe that the development of a standalone, separate standard is not the best solution given the challenges in auditing LCEs, as we deem that the benefits achievable through the greater scalability and proportionality of the ISAs are greater. For the purposes of this consultation, however, we provide our viewpoint on ED-ISA for LCE and agree that it is necessary to regulate the scope of its application.

Given the difficulties in defining the characteristics of an LCE in sufficient detail, we understand the approach applied by the IAASB to instead define the various classes of entities for which it is prohibited to use the proposed standard and the characteristics of the entities that do not qualify as LCEs and for which, therefore, application of the standard would not be appropriate.

However, we have an issue with the general assumption that entities with public interest characteristics, other than listed entities, cannot be considered LCEs and, hence, fall under the specific prohibitions of the proposed standard given the two different categories. Indeed, even if listed companies are excluded, there still can be less complex entities with public interest characteristics. Moreover, the possibility left in the adoption and enactment process to individual jurisdictions to amend (but not remove) the classes of entities as per paragraph A.7 (c) (i)-(iv) - by defining sub-classes - could partly resolve this issue. Although the public interest characteristics of some entities could require the application of rules not currently included in ED-ISA for LCE³, the emphasis on public interest characteristics as the discriminating element in the decision about the proposed standard's scope, considering the intention or requirement to protect public interests, could imply again that the audit of an LCE conducted in accordance with the proposed standard would not give the same degree of assurance as an audit conducted in accordance with the ISAs.

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 Memorandum⁴.

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,

³ For example, in Italy, ISA Italia 701 is applicable not only to listed entities but to all Public Interest Entities (PIEs).

⁴ We refer specifically to the paragraph: "For example, consider the circumstance where an entity has an accounting estimate calculated using a bespoke, complex model that is not contemplated by the proposed standard, but is otherwise an LCE. In this instance, an auditor may not use ED-ISA for LCE together with requirements from ISA 540 (Revised) to supplement what may not be addressed in ED-ISA for LCE when planning and performing the audit."

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.

4. 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:

- (a) Specific prohibitions; and**
- (b) Qualitative characteristics.**

If you provide comments in relation to the specific prohibitions or qualitative characteristics, it will be helpful to clearly indicate the specific item(s) which your comments relate to and, in the case of additions (completeness), be specific about the item(s) that you believe should be added and your reasons.

We set out below some additional considerations about the specific prohibitions and qualitative characteristics and also refer to our more general comments on the Authority in our response to question 3.

The classes of entities for which the use of the proposed standard is specifically prohibited include listed entities and public interest entities, which usually embody a level of complexity for which the proposed standard and its procedures have not been designed.

We agree with the exclusion of listed entities from the proposed standard's scope but note that the definition provided in the Authority Supplemental Guide for such entities (Entities, whose shares, stocks 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) is not consistent with the definition of public interest entities as per European legislation (entities ... whose transferable securities are admitted to trading on a regulated market). The reference to a "recognized stock exchange" rather than a "regulated market" could give rise to interpretative and application difficulties.

We note the IESBA's proposal with respect to the ED "Proposed Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code" issued in January 2021 to replace the term "listed entity" with the new term "publicly traded entity". We agreed with this proposal as long as it is clear that the publicly traded entities solely include those active on a regulated market, as per the above European regulation. Entities active on a "recognized stock exchange" are normally subject to different and less strict rules compared to those applicable

to companies admitted to a “regulated stock exchange”. This choice, adopted in most jurisdictions, aims at creating an alternative to the admission to trading of financial instruments on regulated markets, allowing for less onerous requirements and less complex rules (considering as well, often, the less complex nature of these entities and their smaller public interest) when these instruments are listed on unregulated markets. Consequently, we believe it would not be appropriate to consider entities listed on “recognized stock exchanges” in the same way as those whose securities are traded on “regulated stock exchanges”. Indeed, this would mean not taking into account the significant differences existing among the rules governing those markets, as specifically enacted by local legislators.

With respect to the classes of entities, other than listed entities, indicated in the Authority as entities that usually have public interest characteristics and, as such, are specifically excluded from the scope of the proposed standard, we believe that critical application issues may arise as a result of the choice to define a list of high-level classes of such entities.

We believe that the wording used may be too generic, as it refers to a wide range of entities that cannot always be determined ex-ante with sufficient certainty.

As an example, with reference to paragraph A.7 (c) (i) (An entity one of whose main functions is to take deposits from public) and (ii) (An entity one of whose main functions is to provide insurance to the public), it is not always easy to determine when the activities mentioned therein actually represent the “main function” of the relevant entity. Such an assessment would end up being guided by an unavoidable margin of discretion and could result in an inconsistent application in practice. The Authority Supplemental Guide provides guidance about this as it establishes that professional judgement is used to determine an entity’s main function.

Moreover, since - according to the Guide - the term “one of whose main functions” is used in order to capture entities that have other main functions such as credit and lending but also to exclude those entities for which deposit-taking or insurance is not a main function, the wording used may give rise to different interpretations in the various national legislative frameworks. For example, at the moment, at European level, banking and insurance companies qualify as PIEs regardless of whether they carry out these activities on a primary, secondary or exclusive basis and, therefore, they have to be considered as public interest entities and, hence, excluded from the proposed standard’s scope. This might not be the case in other jurisdictions.

Similarly, the identification of the entities listed under sub-paragraph (c) (iii) of paragraph A.7 (An entity whose function is to provide post-employment benefits) does not appear straightforward and could lead to inconsistent applications, and consequent impacts on the performance of the audit, depending on the specificities of national systems.

It is therefore our view that, in order to avoid uncertainties and the lack of consistency which would result from the introduction of too broadly defined criteria, as explained above, the proposed standard should set out very clearly defined classes of entities where use of the ED-ISA for LCE is prohibited. Alternatively, if the Board wishes to maintain the broad definitions, it should then only set more precise guidelines for the authorities in each jurisdiction, which would have full authority to classify an entity as prohibited from the use of the standard.

Reference should be made to our response to question 22 for our comments on the exclusion of group auditors from the scope of the proposed standard.

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.

5. Regarding the Authority Supplemental Guide:

(a) Is the guide helpful in understanding the Authority? If not, why not?

Without prejudice to the critical issues noted in our responses to the previous questions and with reference to the role assigned to firms to establish possible additional limitations to the use of the proposed standard for certain classes of entities or business sectors as per question 6, we believe that the Authority Supplemental Guide is, overall, useful as it refers to and gives more detail about the considerations made in the Explanatory Memorandum.

Specifically, thanks to the examples provided, the Guide assists the auditor to understand when (due to qualitative characteristics) the use of the proposed standard is appropriate in order to decide whether or not it can be applied to audit a specific entity.

The list of examples of qualitative characteristics of entities, provided by the Guide in order to facilitate an understanding of the appropriate use for a specific engagement, is not exhaustive and the Guide clarifies that other relevant matters may also need to be considered. In addition, both the Guide and the proposed standard clarify that the existence of a characteristic of complexity does not automatically exclude the use of the proposed standard for an entity although, theoretically, this could be the case. Therefore, the matters described in the list are intended to be considered both individually and in combination. However, if there is uncertainty about whether, based on the consideration of typical characteristics associated with complexity, an audit is or is not an audit of an LCE, it is appropriate to conclude it not to be an audit of an LCE and so be excluded from using the proposed standard. Accordingly, application of the full ISAs would be appropriate. Moreover, as already stated, it is clear that, as these assessments are made by an auditor using their professional judgement, their assessment about a specific entity may differ from that of another auditor. This leads us to conclude that it may not be possible to apply the proposed standard consistently.

Nevertheless, in order to minimise the risk of inconsistent application, we recommend operating guides be prepared or that the content of the Authority Supplemental Guide be extended with additional examples that cover:

- those characteristics that determine complexity levels that make it inappropriate to apply the proposed ISA for LCE, with particular reference to characteristics related to the entity's:
 - o business activities, business model and industry;
 - o organisational structure;
 - o ownership and oversight structures;
 - o applicable regulatory framework;
 - o accounting processes;
 - o IT environment and system;
- examples of complex accounting estimates, clarifying whether the following situations fall into this definition:
 - o the measurement (including performance of the impairment tests) of goodwill, intangible assets (especially for start-ups), equity-accounted investments, provisions for risks and charges (for which the entity uses its own experts);
 - o the analysis of business plans and/or budgets to assess the going concern assumption;
- the circumstance whereby the proposed ISA for LCE cannot be applied due to the existence of a single complex accounting estimate or the presence of several complex accounting estimates.

(b) Are there other matters that should be included in the guide?

See our previous response.

6. Are there any other matters related to the Authority that the IAASB should consider as it progresses ED-ISA for LCE to finalisation?

We do not agree with the possibility envisaged in the proposed standard for firms to further limit - in addition to the specific prohibitions defined by the proposed standard or established by local regulations or standard setters - the use of the standard for certain classes of entities or their business sectors by defining internal policies and procedures designed to regulate the application of the draft standard.

Whilst legislative or regulatory authorities or relevant local bodies are best placed to set additional criteria or further prohibitions to that already set out in the Authority, we strongly believe that the firms should not be responsible for determining specific classes of entities to which the use of the proposed standard is restricted. We believe that this will result in inconsistent applications across jurisdictions, networks, countries, etc. resulting from the different choices made by different firms.

In addition, specifically, we do not agree with the emphasis in paragraph 65 of the Explanatory Memorandum (and paragraph 42 of the Authority Supplemental Guide) on the quality risks as a result of the nature and circumstances of the engagements performed as an example for the decision about whether to use the proposed ISA for LCE. This could reinforce the view that an audit of an LCE conducted in accordance with the proposed standard does not provide the same level of assurance as an audit conducted in accordance with the ISAs.

Accordingly, we recommend the approach be reviewed and the statement “The firm may also further limit the classes of entities for which the firm’s engagement teams can use the [draft] ISA for LCE” be removed from paragraph A.12 and paragraph A.13 of the [draft] standard be amended accordingly.

Section 4C – Key Principles Used in Developing ED-ISA for LCE

7. Views are sought on the key principles used in developing ED-ISA for LCE as set out in this Section 4C. Please structure your response as follows:

- (a) The approach to how the ISA requirements have been incorporated in the proposed standard (see paragraphs 74-77).
- (b) The approach to the objectives of each Part of the proposed standard (see paragraphs 78 -80).

We have believed it appropriate to respond to points (a) and (b) together. The methods applied to incorporate the ISA requirements and objectives in the proposed ISA for LCE adequately present the requirements and the objectives as well as describing their scope for the purposes of an audit of an LCE. The presentation by audit process (rather than by individual topic like for the other ISAs) is consistent with the nature of the LCE to which the standard is applicable (the presentation by flow provides a single guide to be adopted in the audit of an LCE).

- (c) The principles in relation to professional skepticism and professional judgement, relevant ethical requirements and quality management (see paragraphs 81-84)

We believe that professional skepticism and professional judgement underpin all audit engagements and are, therefore, fully applicable to the LCEs. However, it would be preferable to explain in the proposed standard that application of due professional skepticism implies consideration of the intrinsic characteristics of these entities and, specifically:

- a) the smaller level of contrary evidence that can be obtained from an LCE as the quantity and quality of the evidence is expected to be less in the case of a smaller entity with less developed internal control systems;
 - b) the greater bias given the limited reporting lines, the possible involvement of the owners in governance and the structure of the LCE. The less complex structure of the LCE effectively reduces the involvement of those charged with governance in company decisions and means that internally-developed assessments are less reliable as they are subjective.
- (d) The approach to EEM (see paragraphs 85-91) including:
 - (i) The content of the EEM, including whether it serves the purpose for which it is intended.
 - (ii) The sufficiency of EEM.
 - (iii) The way the EEM has been presented within the proposed standard.

We believe the approach taken in the proposed ED ISA for LCE to EEM is inadequate. We note that the proposed standard has been shortened mainly by eliminating or moving the guidance that is an integral part of the ISAs to supplemental guides. This means that, in some cases, the proposed standard lacks those guidelines and application examples that are necessary to allow

application of the requirements. In other cases, the removal to supplemental guides (see for example the amendments to the opinion that are mainly treated in the LCE Supplemental Guidance Auditor Reporting) gives these supplemental guides a different authority to that of the ISAs for the same topics.

We recommend that additional guidance be included in the ED-ISA for LCE, including the re-introduction of guidance moved to supplemental guides to the proposed standard. This would make the proposed standard longer but would facilitate its more consistent application.

In our view, the guidance in the EEM does not always seem to relate to the LCEs. The information included in the EEM should reflect the simple and limited nature of their internal control systems and, therefore, allow the easy application of the concepts for this type of entity. The guidance about professional skepticism and professional judgement should be included in the EEM.

Section 4D – Overall Design and Structure of ED-ISA for LCE

- 8. Please provide your views on the overall design and structure of ED-ISA for LCE, including where relevant, the application of the drafting principles (paragraph 98-101).**

The overall design and structure of ED-ISA for LCE achieve the objective of having a single concise and exhaustive guide to the audit of an LCE. However, as we noted earlier, there is a lack of guidance which, if provided, would facilitate the more consistent application of the proposed standard. Specifically, the EEM should provide the auditor with more appropriate and defined explanatory material with information about the characteristics that an LCE should have (simplified internal control system, less reporting lines, etc.) and guidance about how to respond to such characteristics.

Section 4E – Content of ED-ISA for LCE

- 9. Please provide your views on the content of each of Parts 1 through 8 of ED-ISA for LCE, including the completeness of each part. In responding to this question, please distinguish your comments by using a subheading for each of the Parts of the proposed standard.**

The content of the proposed standard is exhaustive for the general parts. Reference should be made to our response to question 7 for the content of the EEM.

Specifically, with respect to section 7 of the proposed standard, the ISA 500 series about audit evidence are particularly sacrificed given their reduction for the audit of LCEs. While Section 7 covers the issue of audit evidence, it does not include the guidance, explanatory material and appendices, especially in relation to the issues covered by ISA 505 (external confirmations), ISA 520 (analytical procedures) and ISA 530 (audit sampling), which are very useful in practical terms. The guidance of these standards and the examples could be included in the proposed standard to make it clearer. Appendix 1 includes a summary of aspects that we believe should be included in ED-ISA for LCE.

10. **For Part 9, do you agree with the approach taken in ED-ISA for LCE with regard to auditor reporting requirements, including:**
- (a) **The presentation, content and completeness of Part 9.**
 - (b) **The approach to include a specified format and content of an unmodified auditor's report as a requirement?**
 - (c) **The approach to providing example auditor's reports in the Reporting Supplemental Guide.**

The presentation of information in tables is consistent with the need for a single guide that includes all aspects of an audit of an LCE. Similarly, we agree with the inclusion of an example of an unmodified auditor's report.

However, as already noted in our response to question 7, the tables in part 9 should be supplemented to provide specific guidance about the type of opinion to be expressed. For example, there are no definitions of "pervasiveness" and "materiality". Therefore, we recommend that the proposed standard include criteria to assist with the decision about the type of opinion to be formed or that the EEM be used to explain the parameters the auditor can refer to in order to decide what type of opinion to express.

The Reporting Supplemental Guide does not currently provide any guidance about how to decide on the type of opinion. Moreover, it is unclear why this Guide is a separate document and is not an "authoritative" guide given the importance of the issues covered (modifications to the auditor's report), especially given its usefulness when modified reports are prepared.

In addition please note that the tables include a reference to note 78 which is not present in the Draft ISA for LCE.

11. **With regard to the Reporting Supplemental Guide:**
- (a) **Is the support material helpful, and if not, why not?**
 - (b) **Are there any other matters that should be included in relation to reporting?**

Please refer to our responses to questions 7 and 10.

12. **Are there any areas within Parts 1–9 of the proposed standard where, in your view, the standard can be improved? If so, provide your reasons and describe any such improvements. It will be helpful if you clearly indicate the specific Part(s) which your comments relate to.**

The proposed standard should include a guide that defines the application methods for the transition from ED-ISA for LCE to the ISAs. See specifically question 13.

Section 4F – Other Matters

13. **Please provide your views on transitioning:**
- (a) **Are there any aspects of the proposed standard, further to what has been described above, that may create challenges for transitioning to the ISAs?**

The existence of qualitative characteristics and specific prohibitions that require consideration when assessing whether to use ED-ISA for LCE imply that a

decision about a possible transition from the proposed standard to the full set of ISAs is left to the auditor. We believe it is inevitable that similar situations may arise which would be treated differently.

Another specific issue related to transitioning that could pose application challenges with respect to Italian statutory audits relates to the preparation of engagement letters. In fact, paragraph 139 of the EM to ED-ISA for LCE states: *If it is determined that ED-ISA for LCE is no longer appropriate for use in an audit engagement, to transition the auditor would broadly need to (as appropriate in the circumstances):*

- (a) *Re-establish the terms of engagement, for example through the issuance of an updated engagement letter. (...)*

This indicates that the engagement letter signed by the auditor and the client should establish the set of standards to be applied and this decision should be agreed by both parties as it is part of the engagement letter. It could imply that the terms of the engagement would have to be renegotiated at every transition and that management of the audit client could refuse them as it could mean an increase in the audit fee due to the increase in the audit work.

The possible scenarios of these circumstances are currently uncertain, also because a change in the reference standards could take place during the audit engagement.

Accordingly, it would appear more sensible to postpone any decision about what set of standards to apply to after the engagement letter has been signed. Therefore, an engagement letter should be prepared that makes provision for when to apply the set of ISAs or when to apply the proposed standard together with agreement about adjustments to the audit fees.

Given that set out above, we do not agree with the wording of point a) of paragraph 139 and believe that specific guidance about this issue should be provided in dedicated section about transitioning (see point b) below).

In addition, we draw your attention to the treatment of transitioning in the auditor's report. To this end, paragraph 140 of the Explanatory Memorandum states:

"The auditor's report should also clearly indicate which auditing standards are used for the period under audit. Where the auditor's report refers to a previous period under audit, for example due to circumstances relevant under ISA 710.35 the auditing standards used for the prior period should also be clearly stated."

If the aim of disclosing the auditing standards used in the auditor's report is to ensure greater transparency about the audit engagement, it would seem appropriate that the proposed standard clarify that, in the case of transitioning from one set of standards to another from one year to the next, the auditor's report should explain the reason behind such transition.

(b) What support materials would assist in addressing these challenges?

Preparation of specific guidance about transitioning in a separate document would facilitate the more consistent management of all issues that could arise when transitioning from the proposed standard to the full set of ISAs.

The Mapping Documents, which compare the ISAs to the proposed ISA for LCE, are a good source of guidance in the case of transitioning.

14. Do you agree with the proposed approach to the future updates and maintenance of the Standard and related supplemental guidance?

We agree with the proposed approach. The proposed ISA for LCE should not undergo much change even if the ISAs are modified given the nature of the LCEs and the fact that these modifications are made mainly to adapt to increasingly specific (and complex) entities.

It would be appropriate that the two sets of standards be kept in line with general requirements, as a difference in requirements would not be understandable and would engender confusion, especially for the users of financial statements and auditor's reports, generating the perception that the proposed ISA for LCE allows for a more superficial audit.

15. For any subsequent revisions to the standard once effective, should early adoption be allowed? If not, why not?

Early adoption should be allowed, like in all other circumstances.

16. Should a separate Part on the ISA-800 series be included within ED-ISA for LCE? Please provide reasons for your response.

Specific information on the ISA 800 series should definitely be included in ED-ISA for LCE.

The current ISA 800 series frequently refers directly and indirectly to other auditing standards. Should an LCE need to have a single financial statement or an element of a financial statement audited (a very frequent circumstance in Italy due to specific laws or regulations or professional practice), the auditor would have to refer to the ISA 800 series and, accordingly, apply all the auditing standards it refers to, with a paradoxical effect given that application of the proposed ISA for LCE excludes the application of the other standards.

17. In your view, would ED-ISA for LCE meet the needs of users and other stakeholders for an engagement that enables the auditor to obtain reasonable assurance to express an audit opinion and for which the proposed standard has been developed? If not, why not. Please structure your comments to this question as follows:

(a) Whether the proposed standard can, and will, be used in your jurisdiction.

Given the Italian business scenario, characterised by numerous SMEs, the proposed ISA for LCE could be widely used. However, due to the requirements for statutory audits, the decision of whether to use the proposed standard in Italy is not within our remit.

(b) Whether the proposed standard meets the needs of auditors, audited entities, users of audited financial statements and other stakeholders.

With respect to users of financial statements, if the purpose is to "enhance the degree of confidence of intended users in the financial statements of an entity" (as stated on page 15 of the Explanatory Memorandum), we are not sure that this objective is achievable with the proposed standard. As indicated in our response to question 1, a possible risk could be a decrease in the confidence in the financial statements on which the auditor's report is issued in accordance with the new standard, especially by users that have less familiarity with the role of auditors.

The reference to this proposed standard risks decreasing the value of the auditor's report and supporting the perception that an audit of an LCE is a more superficial audit (a B series audit).

(c) Whether there are aspects of the proposed standard that may create challenges for implementation (if so, how such challenges may be addressed).

See earlier, including with reference to transitioning.

18. Are there any other matters related to ED-ISA for LCE that the IAASB should consider as it progresses the proposed standard to finalization?

We have nothing to report in this respect.

Section 4G - Approach to Consultation and Finalization

19. What support and guidance would be useful when implementing the proposed standard?

In addition to that set out in our previous responses, we recommend a document be prepared illustrating a practical example of an audit conducted in accordance with the proposed ISA for LCE, using the approach of the Guide to Using International Standards on Auditing in the Audits of Small- and Medium-Sized Entities - Vol. 2 - Practical Guidance issued by the IFAC.

It could also be useful to include examples of audit programmes or checklists to be used for audits of LCEs.

In Italy, auditors are subject to specific legal obligations and dedicated auditing standards have been drawn up which would continue to apply after the necessary modifications.

20. Translations—recognizing that many respondents may intend to translate the final ISA for LCE in their own environments, the IAASB welcomes comment on potential translation issues noted in reviewing ED-ISA for LCE.

We do not foresee any specific translation issues.

21. Effective Date—Recognizing ISA for LCE is a new standard, and given the need for national due process and translation, as applicable, the IAASB believes that an appropriate effective date for the standard would be for financial reporting periods beginning at least 18 months after the approval of a final standard. Earlier application would be permitted and encouraged. The IAASB welcomes comments on whether this would provide a sufficient period to support effective implementation of the ISA for LCE.

ED-ISA for LCE acknowledges the important role that national standard setters will play in further refining the scope and authority for its use in an individual jurisdiction. In our view, a period of 24 months from approval of a final standard would be the minimum period necessary to allow sufficient time to allow for implementation across jurisdictions, including the need for firms to establish policies and procedures once any further implementation decisions by jurisdictional authorities become known.

Section 5 – Group Audits

22. **The IAASB is looking for views on whether group audits should be excluded from (or included in) the scope of ED-ISA for LCE. Please provide reasons for your answer.**

We support the IAASB's view that group audits should normally be excluded from the scope of ED-ISA for LCE, as they inherently embody a higher degree of complexity.

However, we do acknowledge that small groups can exist for which their audit may be deemed less complex. Accordingly, we encourage the IAASB to supplement the existing Exposure Draft with a clear description of the criteria under which the adoption of the proposed ISA for LCE for group audits would be deemed appropriate.

23. **Respondents in public practice are asked to share information about the impact of excluding group audits from the scope of ED-ISA for LCE on the use of the proposed standard. In particular:**

- (a) **Would you use the standard if group audits are excluded? If not, why not?**

We believe that the proposed standard will be used regardless of the inclusion of group audits.

However, the circumstance dealt with at the end of paragraph 157 of the ED, i.e., when a group auditor has to determine whether for the purposes of the audit of the consolidated financial statements the use of the proposed ISA for LCE in the audit of the single components is sufficient, could lead to less utilisation of the proposed standard in the statutory audit of the financial statements of the components. Should the group auditor require the audit of the reporting package prepared for consolidation purposes using the ISAs, it may be inefficient to perform the statutory audit of the financial statements of the same component using the proposed ISA for LCE.

Therefore, if group audits continue to be excluded from the scope of the proposed ISA for LCE, we believe it is necessary for the IAASB to address the question of the auditing standard(s) to be applied for the components of the group. There will be practical implications if the statutory audit of a component can be conducted using the proposed ISA for LCE but ISAs are required, or requested, by the group auditor for audit work at that component due to a requirement to use the ISAs for the group audit opinion.

- (b) **Approximately what % of the audits within your firm or practice would be group audits that would likely be able to use ED-ISA for LCE (i.e., because it is likely that such group audits could be considered less complex entities for the purpose of the proposed standard) except for the specific exclusion?**

Assirevi does not have information on the commercial activities of its members and, therefore, is unable to respond to this question.

(c) What common examples of group structures and circumstances within your practice would be considered a less complex group.

Examples of situations where a group could be considered less complex with the precondition that all its components meet the requirements to qualify as LCEs are:

- the components are all based in the same country and audited by the same network;
- the foreign components are commercial entities only and are audited by the same network;
- the majority of assets and revenue is held/earned by the parent and the other components are immaterial;
- the group operates in just one sector or is subjected to the same regulations;
- the IT systems are highly integrated or their management is centralised with the parent, standard non-customised software is used, external providers are not used;
- the ownership and oversight structures are straightforward (e.g., a group held by a single party or a family), there are no significant related parties;
- the consolidation process is straightforward, is performed at parent level, there is a group manual and standard accounting policies are applied.

24. If group audits are to be included in the scope of ED-ISA for LCE, the IAASB is looking for views about how should be done (please provide reasons for your preferred option):

- (a) The IAASB establishes a proxy(ies) for complexity for when the proposed standard may be used (“Option 1 - see paragraph 169); or**
- (b) ED-ISA for LCE sets out qualitative characteristics for complexity specific to groups (Option 2 - see paragraph 176), to help users of the proposed standard to determine themselves whether a group would meet the complexity threshold.**

Assuming that, as a general principle, professional judgement is to be applied to identify an LCE and, therefore, less complex groups, we prefer the second option.

This approach is also more consistent with the concepts underlying the proposed standard although obviously it requires the use of a higher level of judgement by the auditor, which could lead to a greater risk of inappropriate use and the need for more documentation supporting the standard’s appropriateness.

25. Are there other ways that group audits could be incorporated into the scope of the proposed standard that is not reflected in the alternatives described above? For example, are there proxies for complexity other than what is presented in paragraph 169 that the IAASB should consider?

We have not identified proxies for complexity other than those identified in paragraph 169, also because we do not believe it is appropriate to establish proxies based on quantitative thresholds to be calculated using financial statements captions (such as revenue, total assets, etc.).

26. If group audits are included in ED-ISA for LCE, how should the relevant requirements be presented within the proposed standard (please provide reasons for your preferred option):
- (a) Presenting all requirements pertaining to group audits in a separate Part;
or
 - (b) Presenting the requirements pertaining to group audits within each relevant Part.

While the proposed ISA for LCE is structured using the flow of an audit, we believe the first option is preferable, i.e., the presentation of all the requirements pertaining to a group audit in a separate Part. This is in line with the approach developed in the ISAs (which have a specific standard, ISA 600) and is easier to use both by the auditor that has to audit the consolidated financial statements (as they would find all the requirements in a single Part) and the auditor that only performs the statutory audit (as the related requirements would be less as they would not include those for the consolidated financial statements).

In addition, cross-referencing would be performed in the other parts of the same standard and not in various standards.

Appendix 1

To support our response to question 9, we summarise below the aspects included in some of the ISA 500 series which should be included in ED-ISA for LCE.

With respect to the external confirmations, they are dealt with very generically in the proposed standard (paragraph 7.3.20 and following paragraphs), merely stating that they are audit evidence, that the auditor shall maintain control over the procedure and consider the consequences of a refusal by a client to prepare and send the confirmation requests.

We recommend one or more additional paragraphs be included to specify:

- the definition of an external confirmation;
- its objective;
- how the confirming parties are selected;
- the evaluations of the responses;
- the evaluation of the audit evidence obtained;
- the procedures to be performed in the case of an unreliable response;
- the procedures to be performed in the case of non-responses.

With respect to analytical procedures, the proposed standard (paragraph 7.3.4) requires the auditor to check if they are suitable given their purpose (and the given assertion) and reliable. It also states that any inconsistencies should be investigated.

We recommend one or more additional paragraphs be included to better specify:

- the definition of the analytical procedures;
- their objective;
- when it is appropriate to use them, considering the assertions to be checked;
- the difference between analytical procedures used to gain an understanding of the client and analytical procedures used to obtain audit evidence.

With respect to sampling as part of the tests of controls and substantive procedures, paragraph 7.3.5 and following paragraphs provide a generic description: the auditor should consider the purpose of the audit procedures and determine a sample size sufficient to reduce the audit risk for a certain area/assertion, perform audit procedures and evaluate the results (while making sure the effect of unusual or non-recurring misstatements is not projected onto the entire population).

Once again, we suggest that one or more additional paragraphs be included to cover:

- the objective of the sampling;
- the definition of the sample, its size and selection of the items to be checked, distinguishing between tests of controls and substantive procedures;
- the nature and cause of misstatements and deviations, again distinguishing between tests of controls and substantive procedures;
- the projection of misstatements;
- the evaluation and reliability of the sample results;
- information about factors that affect the size of the sample in the tests of controls;
- information about factors that affect the size of the sample in the substantive procedures.

In addition, the appendices of ISA 530 that illustrate the various methods to select samples could be included.

Finally, we note that the proposed ISA for LCE does not include any specific mention of the audit of inventory and provisions for risks as per ISA 501. The proposed standard (page 30) states that the issues dealt with by ISA 501 are characteristics of more complex entities. We do not agree with this as, for example, the application of ISA 501 to inventory is necessary as inventory is material for financial reporting (ISA 501.4) and this is a circumstance which could also be true of an LCE. With respect to the tests specified in ISA 501 for litigation and claims, we have not identified factors which would make the standard solely applicable to more complex entities.