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Online submission

To whom it may concern

Re: IESBA Exposure Draft: *Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)*

On behalf of the South African Institute of Professional Accountants (SAIPA) we would like to comment on Exposure Draft ***Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)*** published by the International Auditing and Assurance Standards Board for comments submitted by 31 January 2022. We appreciate the opportunity to comment on this Exposure Draft.

General Comments on Proposed ISA for LCE

Response: We are supportive of the development of the proposed ISA for LCE . Smaller, less complex entities (LCEs) make a critical contribution to the world economy and account for the great majority of audits globally. At the same time increasingly complex structures and transactions need to be addressed through the development and revision of the International Standards on Auditing (ISAs). The IAASB recognizes that reflecting this complexity in the ISAs could pose challenges for audits of less complex entities.

We have a few major concerns which are detailed in the sections below, being:

- The Specific Exclusion of Group Audits from the standard
- The application and level of judgement required when considering the qualitative factors which could result in inconsistent application across similar organisations
- Guidance provided on applying the Authority of the Standard
- Awareness of the supplemental guidance for the authority of the proposed standard
- The perception of the standard by all stakeholders and public domain

Specific Questions

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?

Response: We agree and understand that smaller, less complex entities (LCEs) make a critical contribution to the world economy and account for the great majority of audits globally, we agree with the standalone nature of the proposed standard.

We agree that the proposed standard is separate from the ISAs with no intended need to directly reference back to the requirements or application material in the ISAs in its application.

If there is a circumstance that has not been contemplated in the design of ED-ISA for LCE as addressed in the Authority of the proposed standard (Part A), relevant ISA requirements cannot be used to “top-up” ED-ISA for LCE in order to address the circumstance.

The one area of concern we have identified is the initial determination of the appropriateness of applying this standard. It should be clear that the auditor cannot apply the standard and add on additional areas from the ISA’s as this standard is a standalone standard.

It is recommended that Implementation Guidance is issued to support auditors by providing further explanation of the requirements and guidance on which entities to use this standard on and how to apply and guidance on carrying out these audits.

- (b) The title of the proposed standard.

Response: We agree with the IAASB’s view that the title should reflect a new category of international standard that effectively describes the proposed standard, while also making it recognizable as an IAASB standard.

Therefore, it is proposed that the new standard be titled “International Standard on Auditing (ISA) for Audits of Financial Statements of Less Complex Entities (ISA for LCE),”. We agree with the proposed title of the proposed standard.

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

Response: We agree with the Board’s intentions to develop a separate auditing standard that will provide a reasonable assurance opinion, using the concepts and principles already used in an ISA audit (as the ISAs are already designed for the auditor to obtain a reasonable level of assurance).

It was also agreed that it needed to clear in the auditor’s report which standard(s) have been used so that users of the financial statements have transparency as to which standards have been applied in conducting the audit.

It is important that the degree of confidence of intended users in the financial statements of an entity is still the same and that the public does not view an audit opinion based on this standard as a different level of assurance nor as an inferior standard than full ISAs.

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?

Response: We agree with the introduction of a new category of international standard for the proposed standard, conforming amendments to the IAASB Preface will therefore be required.

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?

Response: The Authority of the proposed Standard needs to be sufficiently clear and understandable to auditors to avoid inconsistent implementation of the standard.

It is important to understand the limitations for using the standard because the requirements in the standard have been designed to be proportionate to the typical nature and circumstance of an audit of financial statements of an LCE in the private and public sectors.

The standard has not been designed to obtain sufficient appropriate audit evidence for complex matters or circumstances. The consequence of using the standard when its not appropriate will lead to insufficient audit evidence which in turn would result in an incorrect audit opinion.

To help with an understanding of when the standard is appropriate to use, the IAASB has developed the “Authority” of the standard and the Supplemental Guidance for the Authority of the Standard. We believe its important for auditors to read the standard and the Supplemental Guidance for the Authority of the Standard together in order to determine if the standard is appropriate.

In describing the basis for the determination of the appropriate use of the proposed standard, it is the IAASB’s view that the relevant limitations be designated into two categories:

(a) Specific classes of entities for which the use of the standard is prohibited.

(b) Qualitative characteristics that, if exhibited by an entity, preclude the use of the standard for the audit of the financial statements of that entity because they are indicators of, or proxies for, matters or circumstances for which the standard has not been designed.

Specific Prohibitions

- **Paragraph A6 states: Legislative or regulatory authorities or relevant local bodies with standard-setting authority can modify each class described in paragraph A.7.(c) but a class cannot be removed. The paragraph should clarify on how these authorities and or local bodies can modify these classes.**
- **The use of the proposed standard should not be prohibited when the audit is an audit of group financial statements. We do not support the IAASB view that group audits inherently exhibit characteristics of complexity within an entity and, consistent with other areas of complexity.**

- We agree with Paragraph A.7.(a) of ED-ISA for LCE intention to apply to all classes of entities in a particular jurisdiction where a jurisdiction either does not want to adopt the ED-ISA for LCE, or the jurisdiction specifies other standard(s) instead.

Limiting Use through Qualitative Characteristics

- If the use of the [draft] standard is not prohibited by the specific prohibitions, the auditor have to exercise judgement and consider the qualitative characteristics in determining if the standards is appropriate for the entity.
- The Qualitative Characteristics set out in paragraph A9 of the proposed standard of
 - (i) business activities,
 - (ii) organizational structure,
 - (iii) ownership,
 - (iv) oversight,
 - (v) regulation, etc. are effective indicators against which to measure whether an entity is an LCE.
- Professional judgment is used in determining whether the entity exhibits the qualitative characteristics of a less complex entity and the [draft] standard is therefore appropriate to use.
- We have a concern regarding the level of professional judgement required together with the understanding of the term complex transactions. This could lead to inconsistent application between auditors on very similar organisations.

- (b) Are there unintended consequences that could arise that the IAASB has not yet considered?

Response: Our concerns were raised in 3(a) above

- (c) Are there specific areas within the Authority that are not clear?

Response: Our concerns were raised in 3(a) above

- (d) Will the Authority, as set out, achieve the intended objective of appropriately informing stakeholders about the scoping of the proposed standard?

Response: We believe the Authority achieves the intended objective of appropriately informing stakeholders about the scoping of the proposed standard other than our concern stated in 3(a) regarding the high level of professional judgement required and inconsistent implementation.

Paragraph A6 states: Legislative or regulatory authorities or relevant local bodies with standard-setting authority can modify each class described in paragraph A.7.(c) but a class cannot be removed. The paragraph should clarify on how these authorities and or local bodies can modify these classes.

- (e) Is the proposed role of legislative or regulatory authorities or relevant local bodies with standard setting authority in individual jurisdictions clear and appropriate?

Response: we believe that the proposed role of legislative or regulatory authorities or relevant local bodies with standard setting authority in individual jurisdictions is clear and appropriate

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.

Response:

Specific Prohibitions

- Paragraph A6 states: Legislative or regulatory authorities or relevant local bodies with standard-setting authority can modify each class described in paragraph A.7.(c) but a class cannot be removed. The paragraph should clarify on how these authorities and or local bodies can modify these classes.
- The use of the proposed standard should not be prohibited when the audit is an audit of group financial statements. We do not support the IAASB view that group audits inherently exhibit characteristics of complexity within an entity and, consistent with other areas of complexity.
- We agree with Paragraph A.7.(a) of ED-ISA for LCE intention to apply to all classes of entities in a particular jurisdiction where a jurisdiction either does not want to adopt the ED-ISA for LCE, or the jurisdiction specifies other standard(s) instead.

Limiting Use through Qualitative Characteristics

- If the use of the [draft] standard is not prohibited by the specific prohibitions, the auditor have to exercise judgement and consider the qualitative characteristics in determining if the standards is appropriate for the entity.
- The Qualitative Characteristics set out in paragraph A9 of the proposed standard of
 - (i) business activities,
 - (ii) organizational structure,
 - (iii) ownership,
 - (iv) oversight,
 - (v) regulation, etc. are effective indicators against which to measure whether an entity is an LCE.
- Professional judgment is used in determining whether the entity exhibits the qualitative characteristics of a less complex entity and the [draft] standard is therefore appropriate to use.
- We have a concern regarding the level of professional judgement required together with the understanding of the term complex transactions. This could lead to inconsistent application between auditors on very similar organisations.

5. Regarding the Authority Supplemental Guide:

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

Response: To help with an understanding of when the standard is appropriate to use, the IAASB has developed the “Authority” of the standard and the Supplemental Guidance for

the Authority of the Standard. We believe its important for auditors to read the standard and the Supplemental Guidance for the Authority of the Standard together in order to determine if the standard is appropriate.

We are concerned that not all auditors will consider the importance of the guide and the need to read the guide with the standard.

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

Response: None noted

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

Response: The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements of an entity. The auditor achieves this by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level in the circumstances of the engagement and expressing an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. It is vital that audits conducted in accordance with the new standard will be widely perceived and recognized as producing an audit that is of the same high quality as that of an audit using the full ISAs.

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).

Response: Consistent with an audit conducted in accordance with the ISAs, the intended outcome from using ED-ISA for LCE is an audit opinion resulting for a quality audit engagement that would enhance the credibility of the financial statements for the users thereof.

Many of the basic concepts used in the ISAs to support a risk-based approach have also been incorporated in ED-ISA for LCE.

We support the approach taken by the IAASB as to how the ISA requirements have been incorporated in the proposed standard. The ISAs was used as a departure point and adapted to be suited for Less Complicated Entities.

- (b) The approach to the objectives of each Part of the proposed standard (see paragraphs 78-80).

Response: We support the approach to the objectives of each Part of the proposed standard

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

Response: We agree with the principles in relation to professional skepticism and professional judgement, relevant ethical requirements and quality management

- (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.

Response:

(i) We agree with the approach to the content of the EEM, including that it serves the purpose for which it is intended.

(ii) It is our belief that the EEM is sufficient.

(iii) We support the way that the EEM has been presented within the proposed standard

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, on the application of the drafting principles (paragraph 98-101).

Response: The IAASB aims to set high quality international standards that are understandable, clear and capable of consistent application, thereby serving to enhance the quality and uniformity of practice worldwide. This includes presenting any required actions as clear, understandable and stated as simply and concisely as practical. The use of long or multiple layers of bullet lists is avoided as this may be perceived as a checklist rather than a principles-based approach.

The proposed drafting principles and guidelines being developed under the CUSP Workstream have been used where appropriate in drafting ED-ISA for LCE.

We agree with the overall design and structure of the proposed standard as well as the overall drafting principles.

We welcome the IASB's approach in which the the separate standard would present the requirements for an audit of an LCE based on the core requirements of the ISAs but drafted and presented in a more understandable and straightforward way

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.

Response: Please see response below per Part

Part 1: No comments

Part 2: Paragraph 2.2.2 states the following: “Appropriateness is the measure of the quality of the audit evidence, that is its relevance and reliability in providing support for the conclusions on which the auditor’s opinion is based. The reliability of audit evidence is influenced by its source and by its nature, and dependent on the individual circumstances under which it is obtained”.

We recommend that the section dealing with reliability should be stated under paragraph 2.3.1 which is dealing with designing the audit procedures and determining the reliability thereof.

Part 3: Paragraph 3.2.4 states: *“In taking overall responsibility for managing and achieving quality through direction, supervision and review of the work, the engagement partner shall determine that the nature, timing and extent of direction, supervision and review is responsive to the nature and circumstances of the engagement and the resources assigned, in compliance with the firm’s related policies or procedures, this [draft] standard, relevant ethical requirements and regulatory requirements”*

The sentence structure is not easily read and understandable and should be structured in separate sections.

Part 4: No comments

Part 5: No comments

Part 6: Paragraph 6.3.5 makes reference to “control activities” in the remainder of the standard its referred to as controls in line with the decision made to use the reference controls. We recommend to remove the word activities form 6.3.5 EMM.

Paragraph 6.5.11 states: *“Based on the procedures performed to identify and assess the risks of material misstatement, the engagement partner shall evaluate whether the [draft] ISA for LCE continues to be appropriate for the nature and circumstances of the entity being audited. “*

We support paragraph 6.5.11 but recommend guidance on how the auditor should apply the change in ISA from this standard to ISA.

Part 7: No comments

Part 8: No comments

Overall Comment: It is recommended that the standard refer to the standard consistently throughout. In the current exposure draft reference is made to:

- The [draft] ISA for LCE.
- This [draft] ISA for LCE
- This [draft] standard.

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.

Response:

- (a) We agree with the presentation, content and completeness of Part 9
- (b) We agree with the approach to include a specified format and content of an unmodified auditor’s report as a requirement.

On the Unmodified auditors report under the Basis for opinion paragraph the standard is currently referred to as: *“International Standard **for Auditing on Audits of Financial Statements of Less Complex Entities (the ISA for LCE)**”* This should read: *“International Standard **on Auditing for Audits of Financial Statements of Less Complex Entities (the ISA for LCE)**”*.

- (c) **We agree with the approach to providing example auditor’s reports in the Reporting Supplemental Guide.**

11. With regard to the Reporting Supplemental Guide:

- (a) Is the support material helpful, and if not, why not?

Response: We support the development of the Reporting Supplemental Guide which we believe to be necessary and helpful.

- (b) Are there any other matters that should be included in relation to reporting?

Response: None

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.

Response: No additional comments

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?

Response: We agree and recognize the challenges of transitioning.

Paragraph A.9. in ED-ISA for LCE specifies that “notwithstanding that professional judgment is used in determining whether the [draft] standard is appropriate to use, if there is uncertainty about whether an audit is an audit of the financial statements of an LCE, the use of the [draft] ISA for LCE is not appropriate.”

Based on the above paragraph we believe the standard is clear that if there are any circumstances where the auditor is uncertain if this standard is appropriate, it is not appropriate to apply this standard. We believe that this will decrease the number of audit engagements where the auditor would apply this standard incorrectly.

We do however recognise that this may occur in practice and that organisations change over the years as their business evolve and may later on be classified as a complex entity and this standard will no longer be applicable for such organizations. Under these circumstances guidance should be provided to the auditor with specific reference to the audit report where the previous year were reported on under ISA for LCE and the current year will be reported on under ISA. The impact on opening balances and the report should be considered and guidance provided as to how to apply this change.

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

Response: We would recommend specific guidance material setting out the transitioning in the following circumstances:

- **Transitioning from ISA to ISA for LCE**
- **Transitioning from ISA for LCE to ISA**
- **Transitioning to ISA subsequent to commencing an audit on ISA for LCE when additional complex transactions were identified**

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

Response: We agree with the proposed approach to future updates and maintenance

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

Response: We have no objections on early adoptions

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

Response: We support the IAASB's approach as to the requirements relating to the ISA 800, which have not been included in ED-ISA for LCE as the IAASB agreed to focus on developing an auditing standard for audits of complete sets of general-purpose financial statements of LCEs first. And we recognise that consideration would be given at a later stage.

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.

Response: We believe that the auditing sector and organisations in South Africa can and will use the standard. It will greatly benefit organisations and improve efficiency.

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

Response: We believe the proposed standard effectively meets the needs of auditors, audited entities, users of audited financial statements and other stakeholders.

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

Response: We are not aware of any other aspects of the proposed standard that may create challenges for implementation, other than those challenges addressed above.

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?

Response: All the matters of concerns were noted in the previous areas.

Section 4G - Approach to Consultation and Finalization

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

Response: Implementation guidance to auditors with regards to the applying the authority of the standard and the transitioning of the standard to and from ISA.

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.

Response: We see no concerns around translations.

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.

Response: We believe this would provide a sufficient period to support effective implementation of the ISA for LCE.

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.

Response: We do not agree with the Authority of ED-ISA for LCE specifically prohibiting use of the proposed standard for group audits.

We are of the view that not all groups are not complex and as such cannot be a single approach to all group audits. We therefore implore upon the IAASB to consider a more innovative approach to addressing group audits.

In our jurisdiction majority of organizations structure their group as a subsidiary holding the premises (land and building) from where they operate. This will then qualify as a group and they will be excluded form ISA for LCE under the current exclusions. If the property were based in the operating company, then they would be allowed to apply ISA for LCE. This is an example of a clear example where group companies should not be excluded and can effectively use ISA for LCE.

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?

Response: If group audits are excluded, it will significantly decrease the number of companies who would be eligible to use this standard. I do however believe it will still be used by the remainder of the eligible companies.

(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?

Response: N/A SAIPA is a Professional Body and not a firm or practice

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

Response: In our jurisdiction majority of organizations structure their group as a subsidiary holding the premises (land and building) from where they operate. This will then qualify as a group and they will be excluded form ISA for LCE under the current exclusions. If the property were based in the operating company, then they would be allowed to apply ISA for LCE. This is an example of a clear example where group companies should not be excluded and can effectively use ISA for LCE

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.

Response: We prefer the proposed standard to set out qualitative characteristics for complexities specific to groups.

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?

Response: No other recommendations

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.

Response: We have no strong view, but for ease of reference and use of the standard, our preference is to have all the requirements in a separate part as the considerations related to group would be specific.

Should you wish to discuss the contents of this letter with us, please contact Faith Ngwenya or Leana van der Merwe or Rashied Small on +27 (0)11 207 7840

Yours faithfully

South African Institute of Professional Accountants