September 12, 2019
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Hunter College Graduate Program
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Re: Discussion Paper Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the ISAs

To Whom It May Concern:

The Advanced Auditing class (ACC 775) at Hunter College Graduate program in New York City appreciates the opportunity to comment on this exposure draft.

The class discussed the above proposed exposure draft and have attached our comments. If you would like additional discussion with us, contact Professor Joseph A. Maffia, at 212-792-6300 ext 404.

Sincerely,

Professor Joseph A. Maffia, CPA, CGMA
COMMENTS TO THE INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD ON THE PROPOSED OPTIONS TO ADDRESS THE CHALLENGES IN APPLYING THE ISAS

September 9, 2019

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The Advanced Auditing Class has reviewed the above-referenced Discussion Paper and offers the following comments for consideration by the International Auditing and Assurance Standards Board. Please note that our comments specifically address the questions outlined in the discussion paper. We thank you for the opportunity to comment.

1. Views about how LCEs could be described.

We generally agree with the qualitative measures the IAASB proposes to use to describe an LCE. We also agree with the general approach to use qualitative measures to describe and LCE. However, we feel that providing only qualitative characteristics without additional guidance on applying this information via examples, the information is vague and ambiguous. For example, the IAASB proposes that entities that have “straightforward or uncomplicated transactions” could be defined as an LCE. We feel that enhancing characteristics to further define what the IAASB considers “straightforward or uncomplicated” would remove ambiguity in this characteristic. We propose that five characteristics to consider as straightforward or uncomplicated are:

A. Entities that operate with an ownership structure of less than five owners with low inherent risks
B. Entities that have nexus in a single jurisdiction.
   - Nexus should be considered physical or virtual presence in a jurisdiction (i.e., brick and mortar presence or goods available for sale in multiple jurisdictions"
C. Entities with gross revenue of less than 5 million
D. Entities with no derivatives, business combinations, stock compensation and/or nonmonetary transactions
E. Entities without a complex capital structure such as options, warrants and/or preferred stock

Additionally, we caution the consideration of internal controls in assessing whether to characterize an entity as a LCE. The review of Internal Controls would encourage smaller entities to enhance their internal controls as a cost saving measure and avoid the scale of an audit of a complex entity and instead submit to audit requirements of LCEs. This would prevent additional audit work such as substantive testing. Instead, we recommend considering effectiveness of Internal Controls as part of the audit, but not in determining if an entity should be considered and LCE. We draw your attention to recognizing that LCE’s typically have few personnel that have a wide range of duties and this would encourage them to continue to have
these in place. In these scenarios, internal controls can serve more in form than substance but by having more internal controls auditors can have greater assurance.

2. Challenges related to Audits of LCEs

A. What are the aspects of the ISAs that are difficult to apply

- Language and Basic Approach to all Standards
  - We believe there should be an emphasis on qualitative and quantitative measures used in language to describe the characteristics of all standards. A financial metric that signals financial effect of the entity that will enhance the classification of the entity. For less complex entity standards specifying the proper amount of documentation necessary to fulfil the audit purpose is necessary. It's understandable that an LCE should require less documentation but the question is to what extent? Due to the complexity of an LCE being less extensive ISA should provide guidelines of what documentation provides assurance and increases audit quality. Applying the ISA standards used for complex entity can lead to over documentation that overall will fail to provide clarity and assurance. We acknowledge that this will take up time and need additional support from key players in the audit industry to make these changes to the standards.

  We also believe that IASB should emphasize the importance of scalability of Audits for LCEs. We think that as an LCE grows from less complex to more complex, the audit considerations too will change. Therefore, the scalability of an ISA is less important. Deemphasizing the scalability component of ISAs will also help alleviate driving auditors towards a more ‘compliance with the standards’ approach rather than an approach that encourages the use of professional judgment in determining the most appropriate audit procedures for the specific circumstances.

- Risk identification and assessment
  - We are supportive of the IAASB’s project to enhance the auditor’s risk assessment process. Risk assessment is an integral part to an auditor understanding and assessing the risks of material misstatement. However, we believe ED-315 proposals regarding testing the design and implementation of internal controls is unnecessary both from an Auditor point of view and cost/benefit analysis from the viewpoint of the LCE client. For LCEs and complex entities, we should understand the purpose of these controls. Risks should be assessed at the account level. However, characteristics that define LCE’s are few levels of management with responsibility for a broad range of controls. Therefore, understanding the design and implementation as set out in paragraph 26 is necessary to identify and assess the potential risks of material misstatement in the financial statements. Further we are concerned that regulators will expect the design
and implementation of internal control requirements to be followed regardless of their appropriateness.

3. Factors driving challenges that are not within IAASB’s

A. The focus should be on legal and other requirements for audits. Uniformity across all jurisdictions brings predictability and clarity for auditors and entities. These characteristics allows both parties to operate more efficiently. If jurisdictional audit exemption thresholds were uniform across all international jurisdictions, the creation and implementation of ISAs for LCEs would be much simpler. With uniform rules, the IAASB can focus on a global solution. Further, uniformity also allows for consistency, comparability and common understanding by all stakeholders. Additionally, annual mandated trainings must occur for auditors across the globe to adapt.

In regards to the table titled “Factors Driving Challenges that are not within the Control of the IAASB,” others should be encouraged to act regarding the Education and People as well as Enhanced Accessibility of the ISAs. Within the Education and People row of the table, it is stated that, “. . . a lack of understanding of existing, new or revised ISAs may negatively impact the way that the ISAs are applied.” While this was considered outside the scope of controls for the IAASB, there are still resources that can be set in place in order to decrease the chance of a negatively impacted audit. A course with a test included should be implemented by IAASB for each auditor following their standards, as well as alerts sent to each firm if a standard is added or altered. It is impossible for auditors to actually follow standards if they are not completely aware of them. This idea goes hand-in-hand with Enhanced Accessibility of the ISAs. It is stated in the table that the IAASB is aware of the inconvenience their handbook poses, but feel as though making the handbook more accessible is “outside of the project on audits of LCEs.” Technically, this handbook is crucial to all audits, including LCEs, because auditors will need standards to refer to in order to properly complete the audit. An auditor or audit team cannot provide “robust” audit services to their highest potential if they are spending large amounts of time trying to find a specific standard. It is the IAASB’s responsibility to provide a more efficient way of presenting the information, perhaps technologically with search methods, in order to allow auditors to easily abide by the rules the IAASB sets forth. This is mentioned as well in the Language and Basic Approach to the Standards row of the table, describing that the standards “. . . are not electronic, so navigating is done manually,” which is not only more difficult for auditors to use, but both a waste of time and resources for the firms following these standards.

4. Possible actions

A. Developing a separate auditing standard for audits of LCE’s
   • We believe that separate auditing standard for Audits of LCEs should be used. Further, we would need to consider how to evaluate and clearly define the one that applies most
to the entity. However, we recognize that a separate standard would provide auditors with specific guiding principles to apply directly to LCEs. This would be written specifically for LCEs in mind and appreciate the value and guidance this would bring to the Audit of LCEs. Planning, Documentation and Risk are standards that should be redirected in the case of LCEs. Audit Documentation requirements should be clearer to lead to consistency in compiling the appropriate amount and adequate documentation to reduce the performance of unnecessary procedures and prevent the omission of some that are necessary. Streamlining specific procedures that enables reasonable assurance of a LCEs audit will promote robustness already accomplished within audits of more complex audits without the extensive performance of procedures. Establishing testing threshold and the documentation required based on specified set parameters would provide guidance and set permanent basis that would enable auditors to foresee the extensiveness of the documentation. Internal control testing can be most likely omitted for software that maintain assets with minimal change such as fixed asset of LCE’s.

5. Other Matters that should be considered
   A. Rewriting of the standard for LCEs will be time consuming and may take a lot of time to fine tune the process. It will require a lot of volunteer hours from industry experts. In the long run this will ensure more effectiveness and efficiency in the practice.

We respectfully submit these comments with the hopes that the final decision of the Federation is in the best interest of the profession as a whole. Should you desire further explanations, please do not hesitate to contact us.