



International Auditing and Assurance Standards Board
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Via IAASB website at www.iaasb.org

Dear Board Members and Staff:

Grant Thornton International Ltd appreciates the opportunity to provide input on the International Auditing and Assurance Standard Board's (IAASB) Exposure Draft: Proposed International Standard on Auditing for Audits of Financial Statement of Less Complex Entities (ISA for LCE), (ED-ISA for LCE) (the Proposed Standard).

We commend the IAASB on its efforts to create a standard that can be applied to less complex entities (LCE) and recognise the challenges this has presented.

In our previous response to the Discussion Paper¹ on the possible options to address audits of less complex entities, we did not support the development of a separate standard for the audit of a less complex entity, preferring that a solution be facilitated through amendments to the ISAs and other related actions. We are of the view that the reasons for this preference remain valid and that other related actions undertaken by the IAASB, such as the Complexity, Understandability, Scalability and Proportionality (CUSP) project along with the digitalisation of the IAASB's Handbook are better steps along the road of creating ISAs that are capable of being applied to a broad range of entities.

We do have a number of significant concerns with ED-ISA for LCE, both in relation to the proposals for the Authority of the Proposed Standard and its application.

Authority of ED-ISA for LCE

We have two issues with the Authority of the Proposed Standard. Firstly, and more importantly, is the prohibition of the use of the Proposed Standard for group audit engagements. Many audit engagements performed by firms are audits of the financial statements of a group. We believe that such a prohibition, along with the lack of clarity regarding the use of ED-ISA for LCE for the audit of a component of a group audit engagement, where that component satisfies the criteria to use ED-ISA for LCE, will have a significant detrimental effect on the adoption of the standard. For example, local law and regulation often requires that a statutory audit of a group be performed. In some instances, a group merely comprises a parent company that holds an investment in a subsidiary, which is the operating company. This structure does not make the group complex in and of itself, and as such we

¹ The IAASB's Discussion Paper, Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the ISAs

believe that absent other factors outlined in ED-ISA for LCE that may make the parent company or operating company complex, it would be appropriate to apply ED-ISA for LCE to the group. We understand that these types of groups are prevalent in a number of jurisdictions.

Secondly, we find the levels of prohibition in the Authority to be overly complex and difficult to interpret. As we note in our detailed response below, we do not believe that the Authority, as written, is capable of consistent implementation across jurisdictions, and more importantly within a jurisdiction. We are of the view that it would be preferable to include an Authority that focuses on when the Proposed Standard can be used rather than when it cannot be used, outline the broad criteria for its use and rely on national standard setters to determine how and when it can be used in their respective jurisdictions, given the use of the Proposed Standard, or otherwise, will ultimately be subject to local laws and regulations. We believe that, with their status and knowledge of the local environment, national standard setters are key to the consistent implementation of ED-ISA for LCE should it be issued with the current proposed Authority. For example, we note that the Authority provides a blanket exclusion of use of ED-ISA for LCE for all listed entities. In some jurisdictions, there are a large number of listed entities that are not complex entities and would not meet any other criteria in the Authority that would prevent the entity from being audited under ED-ISA for LCE. For example, junior mining companies are often listed entities but often only incur and report expenditures in their financial statements, making them less complex.

Application of ED-ISA for LCE

The Proposed Standard is currently positioned as a standard that is capable of being applied without knowledge of, or reference to, the ISAs. On balance, we agree that this is preferable, despite reference to the ISAs being a potential means to reduce the instances when transition into and out of the Proposed Standard may be necessary. Assessing whether the Proposed Standard can truly be applied without reference to the ISAs is difficult due to auditors' existing general knowledge of the ISAs. However, initial indications would suggest that there are sections of the Proposed Standard that may not be capable of being applied without reference to the related application material in the underlying ISA. This is particularly prevalent in Part 6 of the Proposed Standard, where we believe that additional, or indeed different, essential explanatory material (EEM) is required to enable consistent and appropriate application of the requirements therein.

What is Different About an Audit Performed Under ED-ISA for LCE

Many of the requirements in the Proposed Standard are exact replicas of the underlying requirements in the ISAs; some requirements in the underlying ISAs have been combined to form one requirement in the Proposed Standard; and others have only been slightly modified from the original requirement to become a new requirement in the Proposed Standard. Outside of ISAs that do not apply in their entirety, there are very few requirements in the ISAs that have not become or formed part of a requirement in ED-ISA for LCE. Whilst this leaves little doubt that if the requirements in ED-ISA for LCE are appropriately complied with, it is capable of providing a reasonable assurance opinion similar to an audit performed under the ISAs, it does beg the question as to whether the auditor will do anything different under ED-ISA for LCE versus full ISAs and therefore whether a separate standard is required.

This lack of modification is particularly apparent in Part 6 of the Proposed Standard in relation to understanding the entity and its environment, and in particular the auditor's responsibilities in relation to understanding internal control and control activities. This was one of the areas of the ISAs highlighted as being more challenging to apply to a less complex entity, yet there has been no discernible change to the procedures that are expected to be performed by the auditor. We recommend that consideration is given to ways in which this Part in particular can be modified further when performing risk assessment procedures for a less complex entity audit and the EEM necessary to support such modified requirements.

Communication

Despite the fact that there appears to be little modification to the audit procedures required to be performed under ED-ISA for LCE, there is the perception amongst some stakeholders that an audit performed under ED-ISA for LCE will result in a reduction of the audit procedures to be performed and therefore a 'cheaper' audit. In addition, there may also be an assumption that the audit opinion under ED-ISA for LCE provides a lower level of assurance. This may, in part, be the result of the differences in the Basis for Opinion section of the auditor's report under ED-ISA for LCE. We would therefore highlight the importance of the IAASB issuing communications detailing or outlining not only what is different about an audit performed under ED-ISA for LCE, but also why use of the Proposed Standard does not result in an audit of a lesser quality or an audit that provides a lower level of assurance.

We attach our detailed response to ED-ISA for LCE, which elaborates on the points highlighted above and which draws on the practical experience of our member firms. We would be pleased to discuss our comments with you. If you have any questions, please contact me or Sara Ashton at sara.hm.ashton@uk.gt.com or at +1 646 825 8468.

Sincerely,

A handwritten signature in black ink that reads "R. Trent Gazzaway". The signature is written in a cursive, flowing style.

R. Trent Gazzaway
Global Head – Quality
Grant Thornton International Limited

Encs: Appendix A: Exposure Draft: Proposed International Standard on Auditing for Audits of
Financial Statements of Less Complex Entities (ISA for LCE)

Appendix B: Parts 1 through 8 of ED-ISA for LCE

The IAASB's Exposure Draft: Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)

The following provides our detailed response to the IAASB's request for comments to the Exposure Draft: Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE).

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

Q1. 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?**

To be capable of being applied as a standalone standard for the audit of less complex entities, ED-ISA for LCE would need to include requirements tailored to the needs of the audit of a less complex entity and clear direction on the application of those requirements through the inclusion of appropriate essential explanatory material (EEM) that negate the need to reference the ISAs. If reference to the ISAs is allowed, as and when the engagement team determines it is necessary, the lines between the requirements and guidance that are relevant to the audit will become blurred and the engagement team's judgment as to which requirements are appropriate will be increasingly open to challenge. It would also be unclear how many times or in how many areas, it is permissible to refer to the ISAs before it essentially becomes an audit under the ISAs.

However, there are benefits from allowing reference to the ISAs where necessary, whilst still allowing ED-ISA for LCE to be used as the primary audit standard. For example, if reference to the ISAs is allowed, it could potentially result in avoiding a situation where the application of ED-ISA for LCE standard is initially determined to be appropriate, however, during the audit, a complex estimate is identified, and the audit then has to be performed under the ISAs, given the audit team would be able to refer directly to the requirements and application material in ISA 540 (Revised)² for that specific aspect of the audit.

There are clearly advantages and disadvantages to both scenarios but on balance, we agree that if a standard for LCEs is to be issued, it should be capable of being applied without reference to the existing suite of ISAs.

Assuming the standard is issued as a standalone standard, we do have concerns that the standard, as currently proposed will be capable of such application. Specifically, we have concerns that the requirements will not be consistently and appropriately applied with the limited amount of EEM included in the proposed standard. The existing suite of ISAs include significantly more guidance on the application of the requirements, and whilst we appreciate some of that guidance is focused on the application of the requirements to more complex circumstances, we believe that substantially more of that guidance would need to be incorporated into ED-ISA for LCE. Auditors who have never performed audits under the ISAs and, over time, auditors that exclusively perform audits under ED-ISA for LCE, will not have the detailed application knowledge of the ISAs and will be solely reliant on the guidance contained within the LCE standard.

² ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

b) The title of the proposed standard.

We have no concerns with the title of the proposed standard.

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

We have no other matters related to ED-ISA for LCE as discussed in the Overarching Positioning of ED-ISA for LCE.

Q2. 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 with the proposed conforming amendments to the IAASB Preface based on the understanding that ED-ISA for LCE will ultimately stand alone.

Section 4B – Authority of the Standard**Q3. 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?**

In our view, the Authority is not capable of consistent implementation. The Authority, as presented, is a multi-level decision tree, which allows for the application of judgment or modification at each of the levels. This can only lead to inconsistencies both across and within jurisdictions, which is contrary to the premise of developing standards that can be applied consistently. We do not believe that this lack of consistency, and therefore lack of comparability, is in the public interest.

In respect of the specific prohibitions, there will likely be variation in the types of entities for which use of the standard is prohibited. This may add an additional unnecessary layer of complexity to performing multi-national group audits, where local statutory audits are performed. Even if ED-ISA for LCE remains prohibited for group audits, certain jurisdictions may allow its use for components of a group that require statutory audits. Further, the prohibition of an entity with 'public interest characteristics' includes a number of criteria that prohibit the use of ED-ISA for LCE based on the 'main function' of the entity subject to audit. There is currently no guidance on how to determine or measure what would be an entity's 'main function.' ED-ISA for LCE also allows for modification of these criteria, albeit through further restrictions, which gives rise to further inconsistent implementation of the standard.

Going down to the next level of prohibitions, there is again jurisdictional level prohibitions. It is not clear what is different between this level of jurisdictional prohibitions and those in the previous level.

There is then yet another level of prohibitions to consider based on firm policies or procedures, that may create yet another layer of inconsistent implementation.

Finally, the prohibitions extend to characteristics of the engagement. The qualitative characteristic of accounting estimates 'subject to a higher degree of estimation uncertainty or ... requires complex methods that may involve multiple sources of historical and forward-looking data or assumptions, with multiple relationships between them' is unlikely to be consistently interpreted and implemented and could have the unintended consequences as highlighted below.

Consequently, we are of the view that a standard developed on the premise of entities for which it could be used, with broad principles that allow local jurisdictions to determine the audits for which the standard could be used, based on local law and regulation, would be much simpler and easier to implement.

However, should the IAASB proceed with the Authority as proposed in ED-ISA for LCE, we believe that the role of the national standard setters will be critical in driving consistency of the application of the Proposed Standard. Further, we would expect that the determination at the firm level of whether ED-ISA for LCE can be used would not be common and recommend that this is reflected in the Authority.

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

We expect that the prohibition of using the standard for group engagements will have a significant detrimental effect on its use. It may affect the adoption of ED-ISA for LCE both by specific jurisdictions and by specific firms, even when its use is permitted by the local jurisdiction. Further, it may promote the continued development of local standards for LCEs that may be applied in group situations.

As noted above, allowing modification at the firm and the engagement level can only result in inconsistent application of the standard. In particular, in this respect, we would highlight using the qualitative criteria of accounting estimates. This could have the following consequences:

- Based on an initial understanding of the entity, no accounting estimates are identified that meet the prohibition criteria. As the auditor continues with the audit under ED-ISA for LCE and obtains an understanding of the entity and its environment, an accounting estimate is identified that makes the use of ED-ISA for LCE prohibited. The auditor then has to switch to the ISAs mid-audit.
- The auditor commences the audit under ED-ISA for LCE, performs planning, risk assessment and some interim audit procedures. Shortly before the period end, the entity enters into a complex financing arrangement, or acquires a new subsidiary. The auditor is no longer able to use ED-ISA for LCE and has to switch to the ISAs after performing a significant amount of work under ED-ISA for LCE.
- In the first year ED-ISA for LCE is effective, the entity qualifies to be audited under the Proposed Standard. In year two, the environment in which the entity operates changes, making use of ED-ISA for LCE prohibited, the auditor therefore performs the audit under the ISAs in that year. In year three, the factors that caused the change in the environment no longer exist and the entity qualifies to be audited under ED-ISA for LCE again. The audit is therefore not being performed under consistent auditing standards.

We are of the view that repeated change in the standards under which an entity is audited would make ED-ISA for LCE undesirable to firms and to users of the auditor's reports. Potentially, firms may find it necessary to develop and maintain at least two methodologies to be prepared for the need to audit under the ISAs; and users would likely not understand why an audit report indicated it was prepared in accordance with the ISAs in one year and ED-ISA for LCE in another year.

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

See our response to parts (a) and (b) above.

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

See our response to parts (a) and (b) above. We are of the view that the scoping of the proposed standard would be understood better by stakeholders if the focus was on the entities that could be audited under the Proposed Standard rather than those that could not be. Users of the auditor's report are unlikely aware of the differences in prohibitions in one jurisdiction compared to another, are unlikely to have a detailed understanding of a

firm's policies and procedures and are unlikely to understand the other restrictions that may prohibit the use 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?

As noted in our response above, it is unclear why there are different levels of legislative or regulatory prohibitions in the Authority. Ultimately adoption and application of a standard will always be on the authority of local jurisdictional regulatory bodies. As noted above, we believe that the jurisdictional national standard setters have a critical role in achieving consistency of adoption of ED-ISA for LCE should the IAASB proceed with the Authority as currently proposed.

Q4. 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

We do not agree with a blanket prohibition to the use of the Proposed Standard for group audits. We are of the view that there are many types of group engagements for which use of the proposed standard would be appropriate. See our response to question 22 below for more detail on the types of groups for which we believe that it would be appropriate to apply ED-ISA for LCE.

Whilst we appreciate the intent of a blanket prohibition for listed entities, we recommend that consideration is given to allowing jurisdictions to determine the types of listed entities that are prohibited from the using the LCE Standard for the following reasons:

- In a number of jurisdictions, there are types of listed entities that are not complex in nature and do not have a board public interest impact. For example, junior mining companies that only incur expenditures.
- For the purposes of applying the requirements of the ISAs, entities that meet the definition of a listed entity may be determined differently. For example, the UK Financial Reporting Council (FRC) excludes stock or debt that is 'in substance not freely transferable or cannot be traded freely by the public or the entity' from its definition of listed entity.

b) Qualitative characteristics.

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

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

As noted in our response to question 3, we are concerned with the inclusion of the qualitative characteristic of accounting estimates. Whilst the concept of prohibiting the use of the Proposed Standard for entities that have accounting estimates with high estimation

uncertainty is a reasonable concept, we are of the view that better guard rails are needed around how and when estimates meet this criterion. Even with the inclusion of the table in the Supplementary Guidance, we believe that this criterion may give rise to inappropriate application of ED-ISA for LCE and can only result in its inconsistent use; both on a period-to-period basis and a firm-to-firm basis.

Q5. Regarding the Authority Supplemental Guide:

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

We believe that the Supplementary Guidance is helpful in understanding aspects of the Authority. However, we would highlight that the need for supplementary guidance itself is an indicator of the complexity of the proposed Authority. Further, the authority of the Supplementary Guidance is not clear. Typically, guidance issued by the IAASB is non-authoritative material. Also, by introducing it as a separate document, it unavoidably results in a certain amount of repetition of that adds to the overall length and complexity of ED-ISA for LCE.

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

As noted above, whilst the table in paragraph 28 of the Supplementary Guidance is helpful, given the judgement that will need to be applied in determining whether an entity maybe audited under ED-ISA for LCE based on qualitative characteristics, examples of how these characteristics should be considered and applied, both individually and in combination, would be helpful.

Q6. Are there any other matters related to the Authority that the IAASB should consider as it progresses ED-ISA for LCE to finalization?

As noted in our response to question 3(a), we are of the view that the Authority should be developed on the basis of when it is appropriate to use ED-ISA for LCE rather than on the basis of when the use of ED-ISA for LCE is prohibited.

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

Q7. 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).

We agree that it is appropriate to use the requirements in the ISAs as a basis for developing the proposed standard for LCE audits. However, we question whether the starting point for determining the requirements necessary for an audit of an LCE is appropriate. The proposed standard has been developed by starting with requirements that exist in the ISAs and making a determination of whether that requirement should or should not be included in a standard for an audit of an LCE. The starting point should rather be to identify requirements necessary for an audit of an LCE, then look to the ISAs to determine whether that requirement exists in the ISAs, then determine whether it is appropriate to incorporate such requirement in ED-ISA for LCE. As a consequence of the approach taken, it is not clear how an audit performed under ED-ISA for LCE would differ from an audit under the ISAs or why a different Basis for Opinion section in the auditor's report for an audit performed under ED-ISA for LCE is necessary.

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

We agree with the approach to the objectives for each Part of ED-ISA for LCE.

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

We agree with the inclusion of the same principles in ED-ISA for LCE as those for the ISAs for the areas of professional skepticism and professional judgment, relevant ethical requirements and quality management given these principles would be equally applicable in an audit performed under ED-ISA for LCE as under the ISAs. Similar to comments we have made previously on recent ISA exposure drafts, professional skepticism is an area where practical guidance on its application and demonstration of such is more valuable than additional requirements concerning its application in audits of financial statements.

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.

We support the intent to keep the proposed standard as succinct as possible by taking a critical look at the guidance that is necessary to support the application of the requirements. We are of the view that the EEM only partially serves the purpose for which it is intended due to its sufficiency, or lack thereof, as noted in our response below.

Further, if the intent is truly to create a standard that is designed specifically for the audit of LCEs, we are of the view that further modifications of the requirements from those as written in the ISAs is possible, particularly in the area of understanding the entity and its processes and performing risk assessments (ISA 315 (Revised 2019)).³

(ii) The sufficiency of EEM.

Whilst we appreciate there is a fine balance to achieve between the length of the proposed standard and the necessary guidance to enable consistent and appropriate application of the standard, we are of the view that the EEM is insufficient to enable consistent and appropriate application of the requirements in Parts of ED-ISA for LCE. This is particularly apparent in Part 6 of the Proposed Standard in relation to the application of the requirements derived from ISA 315 (Revised) 2019.

(iii) The way the EEM has been presented within the proposed standard.

We have no significant comments on the way that the EEM has been presented within the standard. In general, it is helpful to have EEM explaining the context of the section prior to reading the section. Locating the EEM that explains the requirement directly below the requirement, is helpful given its proximity, but is reminiscent of 'pre-clarity' drafting structures and may be somewhat academic if the proposed standard is to be made available in an electronic format similar to the ISAs. We recommend that the IAASB give further consideration to how the digitalisation of ED-ISA for LCE can be used as an effective means of providing sufficient EEM to facilitate the consistent and appropriate application of requirements and, in particular, those requirements that are conditional. Further, if linkage back to the ISAs is to be permitted, this could also be a means of creating that linkage.

³ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment*

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

Q8. 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).

In general, we support the overall design and structure of the proposed standard. Based on our outreach, some found the organisation of the requirements in the sequence of how an audit is performed helpful and instructional, whilst others preferred organisation by topic, consistent with the organisation of the ISAs. We also find the consistent presentation of each of the parts helpful in the navigation of the proposed standard.

The drafting principles are sensible, and we encourage the IAASB to be stringent in its application of those principles. As the CUSP project is still in its early stages, we also encourage the IAASB to reflect updates from this project as the ED-ISA for LCE is finalised.

Section 4E – Content of ED-ISA for LCE

Q9. 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.

Please refer to Appendix B for our responses to Part 1 through Part 8 of ED-ISA for LCE.

Q10. 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.

We support the presentation and content of Part 9 of ED-ISA for LCE. In particular, we support the use of tables to present the auditors options for modifications of auditor's reports, the effect of the modification on the auditor's report and examples of the disclosure under that particular modification.

We are of the view, however, that this Part needs to deal with format and content of the auditor's report in situations where the prior period was audited under different standards than in the current period, specifically if one year is audited under ED-ISA for LCE and the other year is audited under the ISAs.

We also have concerns regarding the proposed content of the auditor's report. We note that the proposed Basis for Opinion section includes a statement that the audit has been conducted in accordance with ED-ISA for LCE. Given the opinion under ED-ISA for LCE is a reasonable assurance opinion, consistent with the reasonable assurance opinion given under the ISAs, we are unclear why this distinction is being made in this section of the auditor's report. Further, as noted above, this may add to the confusion and stakeholders' perception concerning the quality of the audit performed.

b) The approach to include a specified format and content of an unmodified auditor's report as a requirement?

We support the proposal to include an auditor's report with a specified form and content. However, in relation to the disclosure of 'Auditor's Responsibilities for the Audit of the Financial Statements' in the auditor's report, we are of the view that the same flexibility for how this is presented under ISA 700 (Revised)⁴ paragraph 42, which allows certain of the auditor's responsibilities to be described on the website of an appropriate authority with a

⁴ ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

cross reference to that website included the auditor's report, would be appropriate. For many less complex entities, where the owners are more involved with the day-to-day operation of the business, communication of the auditor's responsibilities is often more informal and achieved through the day-to-day interactions between the owners and the auditors.

Whilst we support the proposed approach of a specified form of auditor's report, we note that its presentation in Part 9 results in some 11 footnotes to enable auditors to appropriately tailor the report. We question whether this will be the most effective way to highlight the items that need to be tailored and recommend that consideration is given to ways in which the footnotes could be integrated with the requirements included in Part 9.

c) The approach to providing example auditor's reports in the Reporting Supplemental Guide.

We are supportive of, and see the need for, the provision of example auditor's reports, however, we have no preference as to whether this is located in the Reporting Supplemental Guidance or in an appendix to ED-ISA for LCE.

Q11. With regard to the Reporting Supplemental Guide:

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

We find the Reporting Supplemental Guide helpful.

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

We did not identify any other matters that should be included in relation to reporting.

Q12. 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 improvements. It will be helpful if you clearly indicate the specific Part(s) which your comments relate to.

See our detailed comments under each of the Parts in Appendix B.

Section 4F – Other Matters

Q13. 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 Authority to use ED-ISA for LCE is governed by, amongst other things, qualitative characteristics that pertain to the entity itself and to the financial information of the entity. The application of these qualitative characteristics will be the primary driver for the need to transition into and out of the standard. At present, it is unclear what the frequency of such transition will be, but it is not uncommon for entities to enter into financing arrangements that inadvertently result in complex accounting estimates that would prohibit the use of ED-ISA for LCE, at minimum for as long as the financial arrangement was in existence. As a result, it would be incumbent on all firms to develop and maintain methodologies for audits under both ED-ISA for LCE and under the ISAs.

For certain of the characteristics used to determine whether ED-ISA for LCE is appropriate, changes to those characteristics that may result in it no longer being appropriate to apply ED-ISA are likely to be known well in advance because of the time it takes for such changes to come to fruition. Therefore, transition between ED-ISA for LCE and the ISAs will likely be known before the audit commences. For example, an entity is unlikely to change its organisational structure overnight or enter into complex ownership arrangements without the knowledge of its auditors. In these situations, in addition to

maintaining the two methodologies, as noted above, auditors will need guidance on how the auditor's report will be affected when the audit is performed under ED-ISA for LCE in one year and the ISAs in the following year.

The other aspect of transitioning into and out of the ED-ISA for LCE, is when that transition has to occur during the audit either because of facts unknown to the auditor when the decision was made to use ED-ISA for LCE or because, for example, the entity enters into a transaction during the period that results in an accounting estimate that is subject to a high degree of estimation uncertainty. In these situations, the audit will have commenced using the methodology for the audit of a less complex entity but will need to be completed under the methodology for the ISAs. Many firms use documentation tools that are tailored to the methodology selected at the beginning of the engagement, so such a change of methodologies 'mid-audit' may prove to be more challenging than simply performing the extra audit procedures required under the ISAs.

Given, at present it is unclear what ED-ISA for LCE is driving the auditor to do differently, it is possible that the cost of maintaining two separate methodologies and, where necessary, the cost of transitioning between standards during the audit may outweigh the benefits.

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

We are of the view that certain aspects of the Authority should be revisited, thus enabling transition into and out of ED-ISA for LCE to be a period-to-period occurrence rather than a potential mid-audit occurrence. As such, as noted in our response above, guidance around the presentation of the auditor's report in situations where the audit is performed under ED-ISA for LCE in one year and under the ISAs in a subsequent or preceding year would be necessary.

Q14. Do you agree with the proposed approach to the future updates and maintenance of the Standard and related supplemental guidance?

We agree in principle with the approach to future updates and maintenance of the Proposed Standard, that is, to consider necessary updates to the Proposed Standard as part of a project to revise or develop a new ISA. However, it is unclear whether the effective dates of any changes arising from the ISA projects will be the same for the Proposed Standard as for the ISA. To avoid confusion, we are of the view that the effective date of any amendments that affect both the Proposed Standard and the ISA should be the same.

Q15. For any subsequent revisions to the standard once effective, should early adoption be allowed? If not, why not?

We are of the view that the adoption, or effective date, of revisions to ED-ISA for LCE should be consistent with those for the ISA from which the changes resulted. Therefore, if early adoption is allowed for the ISA, early adoption should be allowed for ED-ISA for LCE.

Q16. Should a separate Part on the ISA 800 series be included within the ED-ISA for LCE? Please provide reasons for your response?

If the separate standard for audits of the financial statements of LCEs is to go ahead, we would support a separate Part on the ISA 800 series to be included. Audits are currently performed under these ISAs and there appears to be no rationale as to why such audits could not be performed in the same manner if the entity subject to audit qualifies to be audited under ED-ISA for LCE.

Q17. 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 response to this question as follows:

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

The ability to use the Proposed Standard, will be a decision that is made by the local jurisdictional regulators. If the proposed standard is not adopted across all jurisdictions, developing and implementing a global methodology for global networks may become problematic and may adversely affect the adoption of the standard by larger firms or networks of firms, especially as many of these networks or firms may have already developed tools and methodologies to scale the application of the ISAs to less complex entities across all jurisdictions. The adoption of the Proposed Standard will also depend on whether the Authority will allow it to be applied to audits of group financial statements and the ability to efficiently transition into and out of the Proposed Standard.

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

It is unclear whether the Proposed Standard will meet the needs of the various stakeholders for a number of reasons.

- The response to the IAASB's Discussion Paper, Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the ISAs, did not indicate overwhelming support for a separate standard for the audits of LCEs.
- Stakeholders in a number of jurisdictions expected ED-ISA for LCE to result in the need to perform fewer audit procedures than in an audit conducted under the ISAs. It is not clear that this expectation will, in fact, be met.
- It is unclear from the Explanatory Memorandum how an audit under ED-ISA for LCE would differ from an audit under the ISAs and what 'reasonable assurance' really means under an ED-ISA for LCE audit, i.e., whether it is the same as reasonable assurance under the ISAs or a level of assurance that is somewhere between the current levels of limited assurance and reasonable assurance.
- Irrespective of the lack of clarity of whether an audit would indeed be different under ED-ISA for LCE, there is the perception that such an audit would involve fewer audit procedures, would provide a lesser level of assurance than one performed under the ISAs and may be of a lesser quality.

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

See challenges described above, in response to the specific questions. We have no additional challenges to highlight.

Q18. 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 no additional matters to highlight.

Q19. What support and guidance would be useful when implementing the proposed standard?

In addition to the areas highlighted above, where we have indicated that additional support and guidance would be helpful, we believe that additional support and guidance is necessary in the following areas:

- The application of qualitative factors to the entity to determine whether it can be audited under ED-ISA for LCE.
- Transition into and out of the Proposed Standard, especially if a mid-audit transition still remains possible.
- Compliance with the requirements in Part 6 of this Proposed Standard, in particular in relation to the IT environment and internal control.
- If the Proposed Standard is permitted to be applied to audits of groups, guidance in relation to the implementation of the recently approved ISA for group audits

Section 4G – Approach to Consultation and Finalization

Q20. 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 the ED-ISA for LCE.

We are not aware of any translation issues.

Q21. 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.

We believe that an appropriate effective date for the standard would be for financial reporting periods beginning at least 24 months after the approval of the final standard. This is a new standard that may require firms to develop a new methodology for the entire audit and not just aspects of the audit, as with the amendment of individual ISAs. It may also require firms to modify existing audit tools that facilitate performance and documentation of the audit.

We agree that it is appropriate to allow early adoption.

Q22. 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.

As noted in our response to question 4 above, we are of the view that it is inappropriate to include a blanket exclusion of the application of the Proposed Standard to group engagements. Not all groups are complex, there are many types of simple or straightforward groups that exist, all for legitimate business reasons. In our view the proposed standard could be applied to the following types of group audits without compromise to quality:

- Groups that comprise a holding company and one (or few) operational subsidiary(ies) and that subsidiary(ies) qualifies to be audited under ED-ISA for LCE;
- Groups that comprise a holding company, one (or few) operating subsidiary(ies) and dormant subsidiaries and those subsidiaries qualify to be audited under ED-ISA for LCE;
- Groups that do not engage in multiple or complex intragroup transactions;
- Groups that are all located in the same jurisdiction and all entities that comprise the group qualify to be audited under ED-ISA for LCE;
- Groups that are primarily audited by one group engagement team or the same office, i.e., the involvement of component auditors is not necessary.

Q23. 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?

If ED-ISA for LCE continues to exclude group audits, we would not be able to use this Proposed Standard for a significant portion of our audit engagements. This, in combination with other prohibitions on the use of the Proposed Standard may make the investment in developing and maintaining a new methodology and updating and maintaining the audit tool exceed the potential benefit. Further, given that the Proposed Standard is effectively a sub-set of the requirements in the ISAs, existing methodologies and tools may already have the ability to scale the audit to LCE engagements.

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?

We would estimate that between approximately 20% to 40% of group engagements would be considered less complex entities for the purpose of the Proposed Standard except for the specific exclusion.

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

Please see our response to question 22 above for examples of group structures that would be considered a less complex group.

Q24. If group audits are to be included in the scope of ED-ISA for LCE, the IAASB is looking for views about how [this] 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.

We are of the view that elements of both Option 1 and Option 2 should be used to establish the authority for when ED-ISA for LCE may be applied to audits of groups. In our view, the characteristics that are ultimately agreed to be appropriate to be used to determine if an entity can be audited under ED-ISA for LCE should be applied to the group in its entirety. If any entity or component possesses a characteristic that prohibits it from using ED-ISA for LCE, then the standard should not be applied to the group audit. Additionally, although these are matters that pertain to the audit itself, rather than to the entity, we are of the view that the location of the component is an important factor in determining whether it is appropriate to apply ED-ISA for LCE, largely for the reasons stated in the Explanatory Memorandum; that the introduction of different local laws and regulations, different cultures and the potential need for translation, all introduce complexities into the audit that may adversely affect the ability to perform a quality audit under ED-ISA for LCE.

Q25. 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 the complexity other than what is presented in paragraph 169 that the IAASB should consider?

See our response to question 24 above regarding the combination of Option 1 and Option 2 presented in the Explanatory Memorandum.

Q26. 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.**

There are advantages and disadvantages to the options suggested above. Including all the requirements in a separate Part to ED-ISA for LCE will result in each Part being longer and requirements and EEM that will not be applicable to all auditors using ED-ISA for LCE. Conversely, including the requirements pertaining to audits of group in a separate Part will result in those auditing groups referring to two parts of ED-ISA for LCE for each stage of the audit. On balance, we prefer the requirements for group audits to be located in the Part of ED-ISA for LCE for which the group audit considerations relate. However, we would highlight that if ED-ISA for LCE is digitised in the same manner as the ISAs, the placement of the requirements and EEM for audits of groups becomes less important.

Parts 1 through 8 of ED-ISA for LCE.

Q9. 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.

We note the following view on each of the parts of ED-ISA for LCE:

Part 1, Fundamental Concepts, General Principles and Overarching Requirements

1.3 Overall Objectives of the Auditor – Paragraph 1.3.3 requires the auditor to ‘determine whether any audit procedures in addition to those required by the relevant Part are necessary to achieve the objectives stated in this [draft] standard.’ We believe that additional EEM is needed in support of this requirement to explain whether this may result in the auditor being unable to use ED-ISA for LCE.

1.5 Fraud EEM – The EEM setting up the context of the section on fraud is somewhat lengthy and duplicative. For example, it repeats part of the objectives of the auditor in *paragraph 1.3.1(a)* and it states twice that ‘misstatements in the financial statements can arise from either fraud or error. Additionally, the final sentence of the EEM may be misleading as it states that, ‘the requirements of this [draft] standard are designed to assist the auditor identifying and assessing the risks of material misstatement due to fraud and in designing procedures to detect such misstatement.’ The Proposed Standard is designed to assist the auditor in identifying and assessing the risks of material misstatement due to fraud and error, not just fraud.

1.5.2 Considerations Specific to Public Sector Entities – The EEM indicates that withdrawing from an engagement may not be available due to public interest considerations. We question whether the audit should be capable of being performed under the Proposed Standard if there are public interest considerations that need to be taken into account.

1.7 Related Parties – The Mapping Documents – ISAs to Proposed ISA for LCE – Document 2 (the Mapping Document 2) includes the requirement in *paragraph 1.7.1* of the Proposed standard to ‘remain alert for information about the entity’s related parties, including circumstances involving a related party with dominant influence.’ This particular requirement is mapped to ISA 550,⁵ paragraph 19, which is a requirement for the auditor to ‘consider ... information when identifying and assessing risks of material misstatement’ when the auditor has identified fraud risk factors. It goes on to explain that ‘a broad requirement to ‘consider’ information relating to related parties when identifying risks of material misstatement has been retained. We are of the view that a requirement to ‘remain alert’ for information is less robust than a requirement to ‘consider’ information. We therefore recommend that consideration is given to revising the requirement in the Proposed Standard.

Part 2, Audit Evidence and Documentation

We have no comments on Part 2 of ED-ISA for LCE.

⁵ ISA 550, *Related parties*

Part 3, Engagement Quality Management

We note that ISA 220 (Revised)⁶ paragraph 24 dealing with situations where the engagement team becomes aware of information that may have caused the firm to decline the engagement had the information been known at the time of acceptance has not been included in the Proposed Standard on the basis that the requirement is addressed through ISQM 1.⁷ It is not clear why this is considered appropriate for ED-ISA for LCE when a separate requirement has been determined to be necessary in ISA 220 (Revised).

We note that ISA 220 (Revised), paragraph 39 requires the engagement partner to obtain an understanding of the information from the monitoring and remediation process of the network and across network firms, yet the ED-ISA for LCE only requires an understanding of this process for 'other network firms.' Other network firms may not be interpreted to include the network as well as the member firms, as such we would recommend terminology between the ISAs and ED-ISA for LCE remains consistent.

Part 4, Acceptance or Continuance of an Audit Engagement and Initial Audit Engagements

We have no comments on Part 4 of ED-ISA for LCE in addition to the comment raised in Part 3 above.

Part 5, Planning

We have no comments on Part 5 of ED-ISA for LCE.

Part 6, Risk Identification and Assessment

Overall, we are of the view that this Part needs to be further tailored to the specific needs of an audit of the financial statements of a less complex entity. As currently drafted, there would appear to be insufficient modification of the requirements to reflect that less complex entities typically have less sophisticated IT environments and that audits of the financial statements of less complex entities are generally more substantive in nature, with significantly less emphasis being placed on controls that the entity may have put in place. For example:

Paragraphs 6.3.6 – 6.3.8 require the auditor to evaluate certain aspects of the entity's internal control system by understanding a number of specified activities. Firstly, we would expect a different level of work effort between a requirement to 'evaluate' and a requirement to 'understand' so the extent of the procedures to be performed by the auditor is unclear; secondly, if the intent was to have a work effort of evaluate, in many audits of less complex entities, a fully substantive audit approach is taken, so there is little to be gained from performing an evaluation of these aspects of the entity's internal control system. We would therefore recommend that these requirements are clarified to clearly differentiate between the elements of the internal control system that the auditor is required to understand and those that the auditor is required to evaluate and the circumstances in which such an evaluation is required.

Paragraph 6.3.14 part (c) requires the auditor to identify controls that address risks for which substantive procedures alone are not enough. *Paragraph 6.5.3* then requires the auditor to determine whether substantive procedures alone cannot provide sufficient appropriate audit evidence for any risks of material misstatement at the assertion level.

⁶ ISA 220 (Revised), *Quality Control for an Audit of Financial Statements*

⁷ ISQM 1, *International Standard on Quality Management 1, Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

There appears to be a degree of overlap between these two requirements, and we question whether it would be possible to streamline. As noted above, audits of less complex entities are often fully substantive audits, therefore it would be helpful to indicate that this situation would not be expected to be common and may be an indicator that it is not appropriate to perform the audit under ED-ISA for LCE. Further, the EEM associated with this requirement provides an example of 'highly automated processing with little or no manual intervention.' This characteristic would appear to be one that would preclude the use of ED-ISA for LCE based on the guidance in the Authority. As such, we would recommend that an alternate example be provided of when substantive audit procedures alone cannot provide sufficient appropriate audit evidence.

Paragraph 6.3.15 requires clarification. It is not clear what 'other aspects' of the IT environment might be, nor is it clear whether the risks referred to in this requirement pertain to the IT applications that support the identified controls or these 'other aspects' of the IT environment. In order to fully understand and apply this requirement, reference to the ISAs would be required.

Paragraph 6.5.6 requires the auditor to determine whether accounting estimates are significant risks. Accounting estimates have been identified as one of the factors that may prevent an audit being performed under ED-ISA for LCE. As such, if an accounting estimate is identified as a significant risk, we would recommend that EEM, or even a requirement, is included in the Proposed Standard that prompts the auditor to consider whether it is appropriate to continue to use ED-ISA for LCE.

Paragraph 6.5.5 allows the auditor to exercise professional judgment in determining whether the assessed risk associated with related party relationships and transactions are significant risks, and *paragraph 6.5.7(b)* requires the auditor to treat identified significant related party transactions outside the entity's normal business as significant risks. We recommend that *paragraph 6.5.5* is placed after *paragraph 6.5.7* and modified to indicate that professional judgment is only applied to those related party transactions that are not required to be treated as significant risks.

Further, we note that the EEM supporting this section is insufficient for the Proposed Standard to be applied without reference to the guidance or application material in the ISAs. Much of the EEM in this section focuses on why the requirement serves a purpose in the audit of an LCE, but does little to inform the auditor on how the requirement should be interpreted. For example, the EEM associated with *paragraph 6.3.16* explains why an understanding of the IT environment is obtained and that the extent of the auditor's understanding will vary based on the nature and circumstances of the firm, but it doesn't provide any helpful guidance on the extent of the work the auditor is required to perform to comply with the associated requirement and in particular, the extent of work required in relation to IT general controls.

A further example of where additional EEM would be helpful is in relation to *paragraph 6.8.1(e)* to provide guidance on the extent of documentation expected in relation to the assessment of the design and implementation of controls.

Part 7, Responding to Assessed Risk of Material Misstatement

We have the following observations in relation to Part 7 of ED-ISA for LCE:

Paragraph 7.2.2(c) requires the auditor to incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures. EEM on how this might be achieved in an audit of a less complex entity, which is often largely substantive would be helpful.

Paragraph 7.3.2(d) requires the auditor to design and perform tests of controls if the auditor intends to rely on the operating effectiveness of the control. We note that identified controls in the audit of a less complex entity are often management review controls, but there is not always documented evidence of that control. We are of the view that it would be helpful to include EEM here that provides guidance to the auditor on how management review controls could be used when testing operating effectiveness.

Test of Controls – This section includes the requirements allowing the auditor to use audit evidence about the operating effectiveness of controls obtained in previous periods, however, unlike ISA 330⁸ paragraph 14, it does not provide a limit on how long the auditor is allowed to use evidence from previous periods before being required to update the testing of the operating effectiveness of the control. We note that the rationale provided in the Mapping Document is that the requirement has been modified for the general circumstances of an audit of an LCE, however, we are of the view that a maximum period of time needs to be established in which the auditor may rely on testing from a prior period and, as such, recommend that a time limit is established in the Proposed Standard, with consideration being given as to whether the three years included in ISA 330 remains an appropriate time period.

Paragraph 7.4.8(b) requires the auditor to perform a retrospective review of management judgments and assumptions related to significant accounting estimates. We question whether, in an audit of an LCE, there should be any significant accounting estimates given this is one of the characteristics that would prevent the auditor from using ED-ISA for LCE.

Use of the Work of an Expert – We question whether the entity is truly an LCE if the auditor finds it necessary to employ an expert in order to obtain sufficient appropriate audit evidence in support of the audit opinion. We therefore recommend that consideration is given as to whether this section of Part 7 is appropriate for an audit of less complex entities.

Accumulation of Misstatements – We question whether it would be better to include this section in Part 8, and specifically in the section containing the requirements for the Evaluation of Misstatements.

Part 8, Concluding

We have no comments on Part 8 of ED-ISA for LCE.

⁸ ISA 330, *The Auditor's Responses to Assessed Risks*