



International Auditing and Assurance Standards Board
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USA

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

The Nordic Federation of Public Accountants (NRF) is pleased to respond to the IAASB's Exposure Draft on *Proposed International Standard on Auditing of Financial Statements of Less Complex Entities (ISA for LCE)*.

General comments

For a long time, audits of SMEs – and especially the challenges of performing such audits effectively and efficiently based on the ISAs – have been a key matter in the Nordic region. Therefore, we welcome IAASB's LCE project and strongly support an international standalone standard for audits of LCEs. Taking into account that the ISAs need to (continue to) address increasingly complex structures and transactions, we believe that a separate standard exclusively focused on audits of LCEs will play a crucial role in maintaining relevance and cost-benefit value of these audits.

When discussing the progress of the draft standard we believe it is also important to bear in mind the rationale behind this project, i.e. responding to uniform global concerns with applying the full ISAs on audits of SMEs/LCEs and the development of a fragmented SME/LCE audit market with a number of national SME/LCE standards. In our view, status quo is no more an option.

At the same time, we believe the draft standard needs more work. It has turned out to be a challenge to understand and explain for relevant stakeholder groups what the differences are between performing an audit of an LCE according to this draft standard as opposed to the full ISAs. In our view, this issue should be further discussed in relation to IAASB's

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Discussion Paper on Audits of Less Complex Entities (the DP) and how the main concerns raised by those respondents have been addressed.

The main concerns with the ISAs raised by the respondents to the DP relate to a) volume, complexity and used language, b) onerous documentation requirements, and c) requirements resulting in certain procedures being performed solely to comply with ISA requirements with no additional assurance or measurable increase in audit quality.

In our view, the draft standard is user friendly. We support the structure of the draft standard and how the concerns in terms of volume, complexity and used language have been addressed.

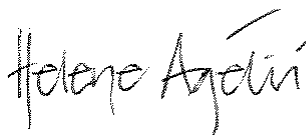
However, in order for this standard to be an attractive and acceptable alternative to applying the full ISAs, we believe more needs to be done in relation to documentation requirements and overly procedural requirements that does not add audit value.

In the explanatory memorandum, the proposed standard is described as a risk-based standard where the exercise of professional judgment has been given a prominent role. We agree with this approach. At the same time, we do not think it is sufficiently reflected in the standard itself. Although a standard for audits of LCEs has a more limited scope than the full ISAs, the LCE audit segment itself also includes a spectrum of entities, where the size criteria continue to be of significance. This is especially apparent in terms of many overly procedural requirements and documentation requirements that have been transitioned into the draft standard from the ISAs. We would encourage the IAASB to further reconsider this, especially how to broaden the application of scalability and proportionality in a way that is better aligned with the risk-based approach to LCE audits. Further room to deal with these matters are particularly apparent in those parts that address the entity's internal control system.

Additional work on these matters would in our view make such a difference in terms of usability while at the same time not impairing the robustness of the standard and the likelihood of reaching the audit objectives.

Finally, we are strongly opposed to the suggested outright prohibition to use the standard on group audits. Excluding group audits from the scope would significantly reduce the usage of the standard in our region.

Yours sincerely,



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About NRF

NRF is a separate legal institution, founded in 1932, acting on behalf of and under the direction of the recognized audit and accounting institutes in the Nordic region (DnR in Norway, FAR in Sweden, FLE in Iceland, FSR – danske revisorer in Denmark and Suomen Tilintarkastajat ry in Finland).

- **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?***

We do support a standalone nature of the standard. The opposite, i.e. not being standalone from the ISAs, would lead to much unclarity and uncertainty, that would impair the usability of the proposed standard. Also, taking into account that the differences between audits of complex global entities and audits of LCEs will most likely continue to increase, moving forward we believe that a standalone standard exclusively focused on this particular audit segment will be of increased importance from both relevance, effectiveness and efficiency perspectives.

At the same time, we are unsure of what is actually meant by “standalone nature”. In particular, our concern relates to how the connection between the ISAs and a standalone standard is described in the Discussion Paper *Audits of Less Complex Entities: Exploring Options to Address the Challenges in Applying the ISAs (the DP)*, and in the Explanatory Memorandum to this ED (the EM). Both papers include statements that a standalone standard should be “based on the ISAs” or “based on the core requirements for an audit within the ISAs, using the concepts and principles already used in the ISAs”.

In our view there is – and should be - a difference between a standard being *based on the ISAs* and a standard that duplicates almost all ISA requirements except those that for obvious reasons are not applicable, i.e. requirements focused on specific circumstances that just do not exist. How to clarify this standalone nature – while still drafting an audit standard that will lead to an audit opinion provided with reasonable assurance – is most likely the core matter in order to create a standard that will be perceived as relevant and that will actually be applied. If practitioners and other stakeholders of the standard cannot see any real differences between an LCE audit performed in accordance with the ISAs or the LCE standard, it will be challenging to explain the need for a separate solution.

Another challenge in this regard relates to application material, which is extensively used in the ISAs, but much less used in the ISA for LCEs. If the standards are too similar, there might be a risk that both auditors and regulators seek guidance in the Application and Other Explanatory Material in the ISAs also when performing, or assessing, an audit under ISA for LCEs.

We strongly encourage the IAASB to look further into this matter. In our view a standalone standard based on the ISAs should not have to follow the ISA requirements to the proposed extent.

We believe the draft standard include some requirements that might not be necessary. Primarily though, we suggest that more needs to be done in terms of both reviewing and clarifying how to apply the LCE standard in a scalable and proportionate way; both in terms of relevant requirements related to the actual audit process, but also to specific documentation requirements within each section.

(b) ***The title of the proposed standard.***

We support the proposed title. In particular, including “International Standard on Auditing (ISA)” in the title is important, since that will serve as a quality mark emphasizing this is a global standard developed by the IAASB.

Similar to the international accounting standard for SMEs: “*IFRS for SMEs*”, we suggest a small amendment in the proposed title so that it refers to LCEs in plural, i.e. ISA for LCEs. The title would then also be aligned with how it is actually being referred to in practice.

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

We would like to stress the importance of clarifying the relationship between relevant requirements “using the concepts and principles already used in the ISAs” and obtaining a reasonable level of assurance in order to achieve a truly standalone standard.

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

We agree with the proposed conforming amendments to the IAASB Preface.

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?**

Taking into account that this is a global standard, we believe the draft Authority strikes a reasonable balance between being too prescriptive and allowing too much judgment. The actual usefulness of the standard will depend on the acceptance and active engagement on national level from especially legislative and regulatory authorities and relevant local bodies with standard-setting authorities.

We anticipate that, at least in the beginning, there might be some inconsistent application, but such inconsistencies should be manageable. Considering that the application of the standard relies on national regulators’ active engagement and supervision, and that the IAASB should not wait too long to perform a post implementation review, any unintended application or major inconsistencies should be able to be dealt with in a timely manner.

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

We have no further comments.

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

In our view the rationale behind the drafting of paragraph A.5. is unclear and confusing. For example, entities that could embody a level of complexity in fact or appearance are not limited to entities with public interest characteristics. Complexity is not even a particular distinctive public interest characteristic. Also, the phrase “in fact or appearance” is mostly used in relation to independence matters. Using that phrase in relation to complexity is confusing and it raises questions, for example, how – and who – should determine whether an entity embodies a level of complexity in appearance? The way complexity is linked to public interest in the prohibition section is not obvious and perhaps not even necessary; most likely the entities covered by A.7. (c) (i)-(iv) would be outside of the scope of the standard anyway based on the qualitative characteristics listed in A.8. and A.9.

In this regard, we do not think that the Supplemental Guidance provides any additional clarity (see also our response to question 5 a). In our view, paragraph A.5. should be deleted.

We believe that paragraph A.6. with its current draft might be redundant and therefore also could be deleted. It is confusing to begin by stating that A.7. sets out the classes of entities for which the use of the draft standard is specifically prohibited – and then move on to state that some of these prohibitions can be modified. Also, this paragraph needs to be read in conjunction to both A.7. and A.11 in order to be fully understood.

One way to clarify this two-tier approach to prohibitions would be to clearly separate the drafting of those entities that are in fact always prohibited from those entities where legislators or regulators can modify the scope. This could be achieved by addressing outright prohibitions in one paragraph (for example in a revised A.6.). The fact that these entities cannot be modified should also be explicitly mentioned in that paragraph. Paragraph A.7. could then deal with those entities which can be modified. That paragraph should also include a reference to A.11.

Paragraph A.9. includes two statements that we believe are contradictory and might confuse the auditors in assessing the applicability of the standard. Firstly, it states that “... LCE is inappropriate for the audit of the financial statement if an entity exhibits one or more of the following characteristics”. In the last paragraph in A.9., it is stated “Each of the qualitative characteristics may on its own not be sufficient to determine whether the [draft] ISA for LCE is appropriate or not in the circumstances, therefore the matters described in the list are intended to be considered both individually and in combination. The presence of one characteristic exhibited by an entity does not necessarily exclude the use of the [draft] ISA for LCE for that entity. 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.” In our view the wording in the first paragraph of A.9. should be changed to correspond with the message in the last paragraph of A.9.

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

We refer to our responses to other sub-questions to question 3.

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

The proposed role of legislative or regulatory authorities or relevant local bodies with standard-setting authority is very similar to the drafting approach used in the IESBA's PIE project. Considering that it is not within the IAASB's mandate to make any demands on this stakeholder group, we believe the proposed role is appropriate.

At the same time, we think the drafting of their role can be further clarified in relation to A.7. For example, we wonder why their role is limited to modifications related to the prohibition section of the Authority and does not include any possibilities to further modify the qualitative characteristics, where relevant.

As further explained in our responses to questions 22-26, we do not support including group audits in the prohibition list as drafted. However, we do understand that striking the right balance regarding how to deal with group audits in a global standard will be a challenge. Groups can be used for different purposes that might even be jurisdiction specific, often group structures are used as a consequence of other national legislation, especially tax law. Taking that into account, we suggest that if group audits – in any form - should continue to be on the prohibition list, they should not be considered as outright prohibitions but rather included in the list of prohibited entities that could be modified by legislative or regulatory authorities or relevant local bodies with standard-setting authority.

Although mentioned in paragraph 17 in the Supplemental Guide, we believe that it could be further stressed in the Authority itself that national legislators etc. could modify the scope by *defining* what entities are covered by the prohibitions. For example, similar language as can be found in the newly approved 400.16 A1 in the Code of Ethics could be used.

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***

We support the prohibitions covered in A.7 (a).

Based on the fact that the ISAs include specific requirements for listed entities that are not duplicated in the draft LCE standard, we also support excluding listed entities in A.7 (b) from the scope.

However, we do have concerns about both the content and the drafting approach in A.7. (b) and (c). As mentioned in our response to question 3 (c), basically we do not believe that public interest entities would need to be singled out in the prohibition list since such entities that are also complex would be scoped out anyway by applying the qualitative characteristics in A.8 and A.9. However, we are ok with including them in the prohibition list as long as these entities are aligned with IESBA's recently approved PIE definition.

The entities covered in draft A.7. (b) and (c) (i) – (iv) are entities that in a broader perspective could be considered as having public interest characteristics. These entities were also included in the IESBA's exposure draft *Proposed Revisions to the Definitions of*

Listed Entity and Public Interest Entity in the Code as proposed entities to be included in a new PIE definition.

At the December meeting in 2021, the IESBA approved of a new PIE definition, that is more limited in scope than the one that was suggested in the ED. Entities whose function is to provide post-employment benefits and entities whose function is to act as a collective investment vehicle and that issues redeemable financial instruments to the public, were deleted from the final scope. Having applied both the same drafting approach and suggested entities in this draft LCE standard, we strongly recommend the IAASB to align the final scope of entities that have public interest characteristics with the IESBA's final PIE definition. For that reason, we suggest that the entities covered by (c) (iii) and (iv) should be deleted from paragraph A.7. as well. If such entities are complex, the draft standard will still not be applicable on audits of such entities due to an application of the qualitative characteristics in paragraph A.8 and A.9.

In the IESBA's new PIE definition, the former sub-group of "listed entities", has now been replaced by the broader term "publicly traded entity", in which listed entities are included. We encourage the IAASB to also consider what impact using that broader term might have in this context, both in terms of whether to include "publicly traded entities" to the prohibition list itself and the possibility for legislative or regulatory authorities or relevant local bodies with standard-setting authority to provide modifications within this category of entities.

Regarding the structure of the entire A.7., we refer to our response to question 3 c).

We agree with the scope itself in A.7. (c) (v). However, at a jurisdictional level we expect this paragraph primarily to be used by setting size criteria *on an overall basis for general application of the draft standard regardless of the entities' public interest characteristics*. We encourage the IAASB to consider whether this broader objective would be clarified if the content in (v) would not be drafted as a sub-group to A.7 (c), but rather be drafted as a separate sub-group to A.7. Also, we suggest clarifying in A.11 (b) that setting specific size criteria could be used as a *general baseline* for use of the standard.

We will comment on A.7. d) group audits separately in our responses to questions 22-26.

(b) ***Qualitative characteristics.***

We believe the specific examples used to explain the characteristics in the first bullet in A.9., i.e. that the standard would be inappropriate to use on audits of entities in new and emerging markets, or entities in the development stage, are too restrictive. For example, one could quite easily argue that many (small and medium sized) entities are in the development stage, even though they in all other matters qualify for the use of the standard. Therefore, we encourage the IAASB to reconsider the impact keeping these examples would have on the use of the standard.

To enhance readability, we suggest adding the word "still" in the intro of A.8: "If an audit engagement is not prohibited from use of the draft ISA for LCE as set out in paragraph A.7., it would **still** be inappropriate...".

5. **Regarding the Authority Supplemental Guide:**

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

Having a Supplemental Guide would be helpful, and we especially support the draft table.

In substance, we encourage the IAASB to further clarify in the table where the threshold is intended to be in relation to the entity's accounting estimates. In our view, the drafted examples are not helpful since they are too obvious. However, if that is the intent, i.e. the examples correctly reflect a "black or white" approach when determining the use of the draft standard, this needs to be clarified. On the other hand, if the standard could still be applicable even though the entity's accounting estimates might involve some level of judgment, this should also be clarified. In case of the latter, we suggest adding some examples that deal with areas such as work in progress, goodwill and real estate.

Overall, we notice that the Supplemental Guidance includes a lot of duplications from the draft standard itself and we wonder how necessary that is. In terms of structure, we also think that the messages in section III *Limitations for Using the Draft ISA for LCE* might be easier to understand if the same drafting approach as in A.11. in the draft standard was used, i.e. by first clearly dealing with situations related to A.11 (a) and then dealing separately with situations related to A.11 (b).

One challenge in the Supplemental Guide is to strike the right balance between clarifying and exemplifying what is in the Authority and adding necessary or new information which should rather be included in the Authority. For example, paragraph 7 in the Supplemental Guidance states: "*Other classes of entities may be able to be "modified" in limited circumstances by legislative or regulatory authorities or relevant local bodies with standard-setting authority*". We believe that the reference to "in limited circumstances" is not reflected in the Authority itself, neither literally nor implicitly. If this is an important message, we encourage the IAASB to consider where the correct placement should be.

Paragraph 8 seems to deal with modifications in general. However, the third bullet refers to using quantitative thresholds to prohibit use of the draft standard *for certain entities*. This message is a bit confusing, especially in relation to paragraph 22 which states that the modifications can also be made more broadly by further prohibiting classes of entities through creating quantitative thresholds. In our understanding the former statement refers to modifications regarding entities covered by A.7 (c) (i-iv) and the latter refers to a general prohibition regardless of the entities' public interest characteristics in A.7 (c) (v). We suggest clarifying these differences.

As mentioned in our response to question 3 (c), this mixture of emphasizing public interest characteristics and complexity has resulted in a blurred message which makes it difficult to determine which factor is the decisive one. For example, according to paragraph A.9 and A.12 listed entities are excluded from the scope of this standard exclusively based on the public interest. Paragraphs 18-20 also focus on public interest characteristics, while the blue box on page 14 regarding Jurisdictional Determinations only focuses on complexity.

Furthermore, paragraph 18-20 refers to modifications that can be made based on an entity's level of public interest characteristics. However, permissible modifications according to paragraph 22 do not seem to take public interest characteristics into account.

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

We have no further comments.

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

We have no further comments.

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).**

We believe the EM includes mixed messages about the relationship between the draft standalone LCE standard and the ISAs. On one hand there are references to the draft LCE standard being “based upon the ISAs”, then again reasonable assurance has been explained as being achieved by “replicating and adapting requirements from the ISAs that are considered core to an audit”. Why all draft requirements are concluded to be core is not further explained.

We believe that the success and actual use of the standard in the Nordic region will depend on how the principles of scalability and proportionality can be used on the draft requirements. In the EM references to these principles are being made primarily in relation to the ISAs and is only briefly mentioned in relation to the use of EEM in the draft standard. Although this standard has a more limited scope than the ISAs, there are still differences between audits within the LCE segment as well. These differences are mainly due to the impact the actual size of the entity has on the audit procedures. In our region statutory audits are mandatory also on micro entities and most of our audit assignments are within this size segment. In our view, the possibilities to use scalability and proportionality need to be further enhanced and also be drafted differently than in the ISAs.

See also our response to question 9 that refers to Part 1 of the draft standard.

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

We support this approach and have no further comments.

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

We support the emphasis on both professional skepticism and professional judgment. Since the exercise of professional judgment is so closely linked to a risk-based approach, we think it would be helpful if the IAASB could further explore and clarify how the standard allows auditors to exercise professional judgment when planning and performing the audit, but also how this concept is expected to be taken into account in regard to the documentation requirements.

- (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.***

The approach to include EEM in the body of the standard and presenting it in connection with the requirements makes the standard reader and user friendly for both practitioners and other stakeholders. However, the positioning of the blue boxes, with different scope depending on whether they occur before or after certain requirements, is confusing and a streamlined approach would be preferred.

Overall, in our view the EEM serves the intended purpose. Although including limited amount of EEM will allow the auditor to exercise professional judgment to a larger extent, there is one area where we think additional guidance could be useful. The application material to ISA 315 (revised) includes many helpful scalability examples. Some of them, but not all, have been incorporated in the draft standard. Depending on the final version of part 6, we would encourage the IAASB to consider adding further examples.

Although we appreciate that the EEM includes examples of scalability and proportionality, we would prefer having these options and conditionality incorporated in the requirements themselves or, even better, redrafting section 1.4 to more generally expand and clarify the use of these principles.

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).***

We strongly support the principle-based approach, the overall design and structure of the different parts in the draft standard. We appreciate that the structure follows the natural flow of audit. With requirements presented in a natural context, the standard is easy to follow and to understand. We believe that the pedagogic way of drafting the standard might actually increase audit quality in these audit assignments, partly since it also encourages the use of professional judgment instead of a checklist approach.

However, referring to our response to question 7 a), we are not convinced that the objectives stated in paragraph 100-101 in the EM have been achieved. One of the main concerns raised by the respondents to the DP was related to the used language in the ISAs. In our view, this specific concern has been addressed in the proposed standard. However, in the

DP other concerns were also raised that were as important and urgent to address, especially concerns around extensive and onerous documentation requirements and requirements that result in certain procedures being performed solely to comply with ISA requirements with not additional assurance or measurable increase in audit quality. It is our view that more needs to be done to address these two areas of concerns.

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.

PART 1: FUNDAMENTAL CONCEPTS, GENERAL PRINCIPLES AND OVERARCHING REQUIREMENTS

Part 1 of the draft standard is of utmost importance since it provides the overall framework within which the standard ought to be applied. We believe this part covers the necessary areas, but at the same time there are some paragraphs that need to be further elaborated on.

In our view, section 1.4 is key for determining whether and to what extent this standard will be applied in practice. As mentioned earlier, even a standard with a limited and focused scope needs to be scalable and proportionate while still ensuring that the objectives of the audit will be reached. The majority of mandatory statutory audits in the Nordic region concerns micro entities. This is also the audit segment where applying the full ISAs is most challenging. The success – and use – of this standard in our region will depend upon its ability to enable the performance of quality audits in an effective and efficient way within this audit segment. Performing certain overly procedural requirements in the draft standard does not make any sense or adds any value to the audits of these entities. Therefore, we strongly recommend that the ability to use scalability and proportionality combined with the proposed emphasis on exercising professional judgment, be both expanded and clarified in the standard.

The definition of “relevant” in 1.4.1 is broad since it is linked to “circumstances that exist”. Often in an audit of a smaller LCE such circumstances can exist without the related procedural requirements having any effect on achieving the audit objectives. In addition to this broad definition of “relevant”, the possibility to deviate from these requirements in 1.4.3 is very limited, especially since the ability to use the exception ought to be based on “necessity”.

In our view, taking into account the risk-based approach in the standard, the exercise of professional judgment in the specific circumstances ought to be included as an added factor in the general description of how to use scalability and proportionality. This could be done, for example, by either including a reference to professional judgment in the definition of “relevant requirements” or by including professional judgment as a relevant factor when determining whether the conditions in 1.4.3 exist. Regarding the exception in 1.4.3, we do not object to the rationale behind the exception, i.e. linking the possibility to depart from a requirement to “specific procedures that would be ineffective in achieving the aim of the

requirement”, but the proposed drafting is unnecessarily limiting. Broadening the possibility to use scalability and proportionality, based on professional judgment, in these specific circumstances, will contribute to more effective and efficient audits of LCEs while at the same time maintaining audit quality.

We suggest that specific documentation requirements linked to the application of section 1.4 needs to be addressed either in Part 1 or in Part 2. Such documentation requirements should also include a statement that clearly not applicable requirements do not require further documentation.

Consistent with our suggested approach, we also believe that the section on “General communications with management and those charge with governance” could be amended in that the auditor throughout the entire standard should be able to use professional judgment in determining the form, timing and content of such communication, especially when there is no particular matter to communicate and/or the matters are routine and simple.

The title of the subsection 1.2.1 refers to “both relevant ethical requirements and firm-level quality management”. We notice that the part that deals with quality management is exclusively dealt with in a blue box, i.e. as EEM which by design is supposed to provide further explanation relevant to a sub-section or a specific requirement, and wonder if this is intentional.

PART 2: AUDIT EVIDENCE AND DOCUMENTATION

One of the areas where the respondents to the DP had most concerns with the ISAs regards documentation requirements that were considered to be extensive and onerous. The feedback we have received in our outreach activities, is that even more could be done in this area.

The draft standard emphasizes the auditor's use of professional judgment in performing an audit according to ISA for LCE. Therefore, we believe that further consideration needs to be done on how to document this, including documentation requirements linked to scalability and proportionality in section 1.4 of the draft standard.

We would also encourage the IAASB to further consider how to address documentation needs for engagement quality procedures. In our view, this is one area where ISA for LCE could clearly mark a distinction between ISA and ISA for LCE, especially in audits of small and micro entities.

Our encouragement to reconsider the documentation requirements also include the specific documentation requirements in the other Parts of the standard, especially since those are even more granular in nature and more focused on documenting procedural actions.

The scope of 2.5.7 is quite broad. In LCEs, and owner managed entities in particular, communication to management and those charged with governance is often informal and oral. Significant communication items would of course require more detailed documentation and often in writing, while other communication tends to be more of compliance nature. We suggest that this is further elaborated on in EEM to this paragraph.

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The second paragraph in the EEM to section 2.5 refer to oral explanations. This sentence is not fully aligned with ISA 230.A5, in that it does not include the end of the sentence: "... but may be used to explain or clarify information contained in the audit documentation." We believe this is important and suggest that it should be added to the EEM. Oral explanations can be very important in an external quality inspection.

PART 3: ENGAGEMENT QUALITY MANAGEMENT

Many SME/LCE audits are carried out entirely by the engagement partner (who may be a sole practitioner) or by a small audit team (who may be small or medium-sized practitioners). Most of these engagements may not be subject to a separate engagement quality review. For quality management, small and medium-sized practitioners will most likely have less formal processes that are supplemented by other sources such as guidance from professional accounting organizations and consulting colleagues in other firms.

Therefore, we recommend the IAASB to restructure the requirements in section 3.2 (The Engagement Partner's Responsibilities) starting from a simple case scenario. Requirements referring to the firm's or network's monitoring and remediation processes and engagement quality reviews should be presented as conditional requirements at the end of this section. Overall, such a drafting approach throughout the standard should in our view be further considered by the IAASB since that would probably more easily capture the characteristics of audits of LCEs.

If firm policies require an engagement quality review, this could be an indication that the audit is complex. At the same time the reason to appoint an engagement quality reviewer can be to respond to other risk management reasons, e.g. initial audit, audit performed by an auditor with recently obtained signing rights or similar reasons. We suggest that the EEM is expanded to explain this.

PART 4: ACCEPTANCE OR CONTINUANCE OF AN AUDIT ENGAGEMENT AND INITIAL AUDIT ENGAGEMENTS

We have no specific comments.

PART 5: PLANNING

We believe there are requirements in this Part where the ability to use scalability and proportionality should be clarified, for example:

5.2.2 EEM: The intention in the EEM is good and relevant. However, we suggest changing "... a brief memorandum prepared **"at the completion"** of the previous audit ..." to **"after the completion"** to avoid unnecessary time constraints for the practitioners.

5.2.6 Engagement Team Discussion: The requirement should allow for audit teams with only 2-3 persons to use a more simplistic approach.

5.2.12 Going Concern: Many of these smaller entities have very informal procedures for assessing going concern. They also have stable secure operations with low risk regarding

going concern. We suggest that the standard clarifies that such assessments does not have to be written.

5.4 Specific Communication Requirements: Taking into account both that most LCEs are smaller in size and that the subject matters of this particular communication requirement often, based on the specific circumstances, are informal and oral, we suggest that this should also be reflected in this requirement.

5.5 Specific Documentation Requirements: The IAASB should reconsider the documentation requirements in 5.5, especially those in 5.5.1. and how those could be applied proportionately in an efficient and relevant way for LCEs that are also small in size. Also, we suggest that the requirement in 5.5.1. to document changes is amended to include an “if applicable”.

PART 6: RISK IDENTIFICATION AND ASSESSMENT

One main concern with the ISAs that was also highlighted in the responses to the DP was “requirements that result in certain procedures being performed solely to comply with ISA requirements with no additional assurance or measurable increase in audit quality”. We believe Part 6 of the draft standard is an area where more could be done in this respect, taking into account the specific characteristics of audits of LCEs, and also by applying scalability and proportionality.

We encourage the IAASB to reconsider the drafting of the requirements in this Part, and especially with regard to section 6.3, for example by considering the following:

6.3.6 Control environment: LCE audits are often performed by using only substantive procedures. While the auditor needs to understand the business processes to perform an effective and efficient audit, in many audits of less complex entities the auditor does not necessarily need to fully understand all aspects of internal control. This is an area where simplifications would be welcome. In our view this requirement should allow for proportionate application taking into account smaller LCEs.

6.3.11. Most LCE entities in the Nordic region are smaller in size and have very informal routines, for example, they do not have formal/written routines for the “information system and communication”. We suggest that this circumstance should be taken into consideration when drafting this requirement.

6.3.17. Use of service organizations: Service organizations mostly used by LCEs are probably external accountants. These are service providers, from which the auditors rarely have problems obtaining audit evidence. Often, an evaluation of the accountant in accordance with ISA 402 does not add much to the audit, which is why we think simplifications would be appropriate. For example some examples of situations where a service organization is not acting as such after the standard.

Compared to other Parts of the standard, more EEM is included in Part 6. We concur the need for more extensive EEM in the important risk assessment phase of the audit as included in the proposed standard. ISA 315 (revised) has many good examples of

scalability. For example, the first bullet in ISA 315 A170 is relevant for many LCEs and we suggest including that in relation to 6.3.11.

6.4.2. The structure of 6.4.2 is similar to the ISAs in that the risk for fraud in revenue recognition is presumed to be significant (ISA 240 p. 27). The client's adherence to laws and regulation, including risk assessment related to fraud in financial reporting is an essential part of the audit. This risk needs to be assessed and adequately responded to. However, having the fraud risks specifically linked to revenue recognition can be misleading in the risk assessment. We suggest that the presumption on fraud in revenue as a significant risk is taken out of ISA for LCE, but that the risk of fraud still needs to be assessed given the circumstances in the audited entity.

6.5.7: According to the proposed standard the presumed significant risk in revenue recognition is a significant risk that can be rebutted. We suggest adding "if not rebutted" in 6.5.7 (a) (ii). We refer to our comment to 6.4.2 where we suggest that revenue recognition should not be a presumed significant risk.

6.8 Specific Documentation Requirements: The general introductory EEM in the first blue box include important information that should not be limited to this part of the draft standard, but could rather be considered to be applied throughout the entire standard. The documentation requirements in this Part are very granular and detailed, for example, the ones in 6.8.1.(a). We would appreciate a reconsideration of these requirements that clearly allows the use of scalability and proportionality. Furthermore, any changes to Part 6 should be reflected in section 6.8.

PART 7: RESPONDING TO ASSESSED RISKS OF MATERIAL MISSTATEMENT

The order of obtaining audit evidence in the ISAs is first through Test of Controls and then through Substantive procedures (substantive analytical procedures and test of details). In Part 7 the order is the opposite, except for in the EEM to 7.3.1. We think that the order of planned response to the risk of material misstatement should be consistent throughout Part 7 and preferably aligned with the order presented in the ISAs.

We suggest that 7.4.8. (b) (ii) could be moved to the risk assessment in part 6 since this could be performed in that phase of the audit.

We suggest that the IAASB reconsider the requirements both in ISA 501 and in 7.4.19 of the proposed ISA for LCE to better correspond with how management determines existence of inventory. Inventory should be treated as any other balance in respect of assessing the risk and audit response to the assessed risk. As such, attending inventory count could be, but does not have to be, an important audit response both from an internal control review procedures perspective and from a substantive procedures perspective and could form part of the auditor's collection of sufficient and appropriate audit evidence. In our view attending physical stock take should only be required if inventory is a significant account balance, i.e. when there is a relevant assertion related to existence. However, if the IAASB determines to keep the requirement as drafted, we would still suggest the requirement to attend management's physical count should be removed in order to allow more flexibility for the auditor.

PART 8: CONCLUDING

Obtaining a written representation is a standard audit procedure. In many countries the law requires management to not withhold any necessary information from the auditor. Furthermore, management and the Board of Directors are required to sign the financial statements. In such situations and from an audit evidence perspective, the added value from obtaining proposed written representations can be questioned. Taking this into account but at the same time acknowledging the *informative* value of written representations, we suggest that the requirements in section 8.6 should be based on a risk assessment.

We believe that both 8.5.2 (c) and 8.8.3 are redundant since the same requirements are already covered by 8.5.5. and 8.8.2. (c) and (d) respectively.

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.**

- (a) We agree with the approach taken regarding the presentation, content and completeness of Part 9. However, paragraph 9.6.3 compared to ISA 710.13 lacks the words: "...and decides to do so...". We strongly suggest adding this since not including that would have a massive effect on an auditor's reporting.
- (b) Already under the ISAs the templates available are used more or less as specified formats amended to reflect specific circumstances (i.e. ISA 570, ISA 701, ISA 720, modifications and other amendments under ISAs). In our view the intention should be the same under ISA for LCE.

In terms of referring to ISA for LCE in the audit report, we recommend the IAASB to carefully consider the pros and cons of doing so bearing in mind that audits of LCEs according to the ISAs or to this LCE standard will both result in the same audit opinion. We recognize that reference to ISA for LCE has an undisputed value from a transparency and full disclosure perspective. At the same time there might be unnecessary negative consequences such as discussions about audit fees and the robustness of the standard (an A or B audit); both factors that might affect the use of the standard.

In the auditor's report there is no possibility to refer to a website for the auditor's responsibility. In the same way as with audits according to the ISAs, we suggest that a reference to a website should be allowed.

- c) We believe the examples are helpful for practitioners and we support providing them in a Reporting Supplemental Guide.

11. With regard to the Reporting Supplemental Guide:

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

We agree that the Reporting Supplemental Guide is helpful, especially we appreciate the structure where mandatory sections that cannot be amended are clearly separated from other sections.

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

We have not noted any such matters.

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.

We refer to our responses to question 9.

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?

Transitions between ISA for LCE and ISA will probably be relatively rare. When there is a need for transitioning, there are aspects to consider that have not been commented on in the EM, for example:

- If prior year was audited according to ISA for LCE and current period according to ISA, will the auditor have to comment on this as “other information” as is expected according to the ISAs when prior year was not subject to audit or if that audit was performed by another auditor? This should be addressed in the ISAs as well. Further, will the opening balance need to be (re)audited according to ISA as well, as required in ISA 510?
- Would it be possible to use ISA for the group audit and ISA for LCE for the individual entities if the need for transitioning is because the LCE has established a group? This is relevant in case group audits will not be allowed under ISA for LCE.
- The EM does not comment on transitioning from ISA to ISA for LCE. Since these are two different standards this should be briefly commented as well.

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

In our view IAASB should issue non-authoritative support material to assist practitioners in transitioning from ISA for LCE both during an ongoing audit and when the transition is made between two financial years.

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

This is an important matter. As stated in paragraph 144 in the EM, recent changes to the ISAs are more directed towards audits of PIEs and complex entities. When changes are made in the ISAs it is important that those changes are analyzed and challenged based on the characteristics of LCEs before being added to ISA for LCE. This might over time result in increased divergence between the standards, which in our view could be justified.

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

Yes, early adoption should be allowed.

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

ISA 800 and ISA 805 reports are also used with regard to LCEs for various stakeholders, such as for agencies providing grants or government support requiring that the receiver of the grant reports the usage of the resources obtained and that these reports are subject to assurance by an auditor. These assurance engagements are often based on the statutory audit performed with added procedures adequate for the circumstances. Moving forward, it would be helpful to further explore the possibilities of linking ISA for LCEs to ISA 800 and ISA 805.

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.

The usability of the standard will be determined by local authorities and market demand.

In the Nordic region there is a demand for quality audits of (smaller) LCEs, that at the same time can be performed in an effective and efficient manner. A standalone standard that exclusively focuses on these audits is therefore very welcome. However, most likely, more work needs to be done on the draft standard in order to become an attractive alternative to the ISAs. In our view, using a risk-based approach that clearly allows scalability and proportionality based on professional judgment, especially where overly procedural requirements are concerned, is both doable and necessary in order to create a standard that will actually be used in practice.

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

The proposed standard is a step in the right direction. The structure and language used in the draft standard will increase the understandability of the audit process itself and might

therefore in itself contribute to higher audit quality. However, as mentioned, more needs to be done with regard to both content and scope.

Moving forward, we also believe that the IAASB will play an important role in informing stakeholders that the audit quality is not compromised when applying this standard.

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

We refer to our responses to questions 1 and 3.

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?*

In the finalization we find it important not to add requirements in ISA for LCE unless absolutely necessary.

Section 4G - Approach to Consultation and Finalization

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

Without priority:

- Information material to external stakeholders from IAASB in order to highlight the existence of the new standard and what an audit according to the standard means for the audited entities.
- Support guidance or documentation examples for where the auditor has used professional judgment.

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.*

Translations are always a challenge. The proposed standard as well as the ISAs are originally written in English. Quite often the English language is richer and have more than one word to express quite similar but slightly different situations etc., while other languages might only have one word to cover a range of nuances. In other words, these nuances will be lost in translation. To the extent possible we encourage the IAASB to keep this in mind when drafting.

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.*

We believe the suggested period for the effective date is sufficient. However, since the applicability of the standard will be voluntary, the effective date is less important.

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.

There are many groups that are not complex and are created based on other reasons than extensive M&A activities. Therefore, the LCE standard should be applicable for audits of Less Complex Groups (LCG).

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?

In the Nordic region, excluding group audits from the scope of the ED-ISA for LCE would result in significantly less usage.

One matter that should be addressed is whether ISA for LCE can be used for the audit of the parent (and subsidiary) but ISA should be used for the group audit. The use of ISA for the group audit could be based on either the (proposed) prohibition to use ISA for LCE or due to the fact that the group audit is complex.

We also think that the IAASB should encourage use of the standard for subsidiaries/ components also for group reporting purposes if the Authority allows the use for the individual company. Otherwise there is a risk that the ISA for LCE will not be used on referred-ins because the group auditor demands an ISA audit.

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 do not have this information available.

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

- Simple structures often created for tax reasons, such as having a specific asset, for example, a real estate property in a separate entity.
- A holding structure to prepare for change in ownership due to retirement or sale of the company (non-complex transaction). These set-ups are often tax driven.

- Subsidiaries (components) that are not material components, i.e. groups where the parent company is the dominate part of the group and where, for example, there is a smaller sales company in another country.

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.**

In our view (b) is the preferred method allowing the auditor to use professional judgment in determining if ISA for LCE (LCG) is applicable. Circumstances to consider in determining complexity in a group:

- Who is auditing the subsidiaries in the group (same auditor, same network, other territory)
- Complexity in the group accounting (valuation, acquisitions/divestments, contingent payments)
- Number of entities in the group
- Existence of significant components (size or risk)
- Applied financial reporting framework, both for the group financial statements and for the components.

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

We refer to our response to question number 24.

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.**

Including the requirements throughout the standard would make the standard more complex to apply for a single entity. Therefore, we find that a separate part is the preferred option.