



IAASB Request for Comments on Audit standard on Less complex entities

Swedish National Audit Office would like to congratulate IAASB for great work done so far. We find that this is a necessary step forward for auditing less complex entities.

With that said we have raised a number of issues in our response to your questions. The most relevant issue is the limitation section. We also believe that the level of detailed requirements could be lower if the limitations section more clearly excludes entities with significant risks.

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

I. 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?
- (b) The title of the proposed standard.
- (c) Any other matters related to ED-ISA for LCE as discussed in this section (Section 4A).

Response:

We support the standalone approach as this is the most comprehensible way.

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

Response:

Yes.

Section 4B – Authority of the Standard

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

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

Response

We believe that the authority section is the most important part of the standard, as the limitations of its applicability would also drive the level of audit requirements. If you only allow the standard to be used for low-risk entities the audit requirements could be less detailed. Of course, not to that extent that it would affect the audit quality negatively.

The most unclear part is the **Limitations** section which could impact the implementation of the standard. This lack of clarity could lead to unintended consequences such as

- difficulties in applying the standard in the public sector
- a variety of different interpretations of when the standard is applicable due to unclear definitions.

As public sector auditors we would like to highlight that the limitations given may lead to an interpretation where you exclude the standard from being used in the public sector. Our environment is quite different from the private sector and there are also differences between different public sectors. The limitations are problematic, mainly because of:

- using the reference to public interest
- stating that the standard may not be used for entities whose main function is to take deposits from public funds.

You may find our detailed comments on the limitation section as response to question 4.

Section Firms and auditors address the responsibilities of the audit firm for the implementation etcetera. It is unfortunate that the public sector is not addressed in this section. We would suggest that you address public sector auditors in this section. For example, it could be highlighted that

- public sector auditors (such as Supreme Audit Institutions) are responsible for implementing procedures etcetera,
- public sector audits or public sector audit standard setters (if they exist) are responsible for defining their own limitations for the use of the standard, based on the suggested criteria in this standard.

4. Do you agree with the proposed limitations relating to the use of ED-ISA for LCE? If not, why and what changes (clarifications, additions or other amendments) need to be made? Please distinguish your response between the:

(a) Specific prohibitions; and

(b) Qualitative characteristics.

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

Response:

The limitations section is complex and difficult to understand. As **public sector auditors** we would like to highlight that the limitations given may lead to a situation where you exclude the standard to be used in the public sector. Our environment is quite different from the private sector and there are also differences between different public sectors. The limitations are problematic mainly because of two factors:

- using the reference to public interest in A5.
- stating that the standard may not be used for entities whose may function is to take deposits from public funds.

First of all, we are not objecting to using reference to public interest, but we would like to underline that this may have an implication for implementing the standard in the public sector.

Public interest

The draft refers to **public interest** in A5. All entities within the public sector have some level of public interest, otherwise they would not exist. This applies even if they are very small and non-complex and it is very important that the standard does not become too prescriptive outing any use in the public sector.

Unclear definitions and terminology

The other criteria for when the standard should not be used is a bit unclear and could also have an impact on the implementation in the public sector. We refer to the criteria in 51 c). or A7 part c. in the draft

(c) An entity meets one of the following criteria:

- *An entity one of whose main functions is to take deposits from the public;*

Almost all our entities are funded by public funds. This could imply that the standard would not be applicable in the public sector. There are terms used which we have difficulties in understanding such as

- “main function”. What would main function mean in practice?
- post-employment benefits. What falls into the category of post-employment benefits. For example, post employee-benefits could be standardized in some jurisdictions and imply low risk from an accounting perspective depending on how you define post employee-benefits.

In general, we agree that the standard should not be allowed in the public sector

- for group audits
- where the law/regulations prohibit it.

Our suggestion

To ensure that the standard is applicable in the public sector we would like to suggest that you clearly state that any public sector auditor such as supreme audit institution may define when the standard is applicable or not depending on the specific audit environment. We would suggest avoiding using expressions and wordings which could lead to the standard not being applicable in the public sector. Terminology used should be defined and clear.

In addition, we would suggest that the standard to a larger extent focuses on disqualifying entities with significant risk. This could be done under the qualitative factor section (A8-A9) by stating that entities with for example the following risks should be excluded:

- significant risks in general and especially risk for accounting estimates
- potential risks for going concern, fraud
- large and complex transactions with complex accounting principles.

The circumstances in paragraphs A8–A9, describing the qualitative factors, are quite many. We think that there should be some additional clarification where the auditor needs to consider an overall conclusion taken all the factors into consideration.

5. Regarding the Authority Supplemental Guide:

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

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

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

Response:

Yes, it is helpful, though our comments on the limitation section apply for the supplemental guidance as well. We suggest that you clarify that it is possible to use the standard on component level within a group audit.

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

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

(a) The approach to how the ISA requirements have been incorporated in the proposed

standard (see paragraphs 74-77).

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

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

(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.

Please note that Section 4E below addresses the content of ED-ISA for LCE, including specific questions for respondents to provide their detailed comments on the content of the proposed standard.

Response:

We agree with your approach using the objective from each ISA. A general reflection is that the requirements in the LCE are basically the same as in the ISA:s. We do not see the real difference between the LCE and how we apply the existing ISAs when auditing a small entity with few employees and a limited budget. The only difference we can note is that we can do mandatory substantive procedures for material accounts (no risk) by either doing test of detail or substantive analytical procedures.

The principles for professional judgement and skepticism are fine.

We find the EEM to be helpful. Though some of the EEMs placement could be discussed. We think that the EEM should follow a requirement and not the other way around. In our comments on the content section 4E you will find our suggestions. Whether they are sufficient or not will depend on how much understanding of the underlying ISA the auditor has. The question is whether the auditor would understand the scope of each requirement if they haven't performed a full ISA audit.

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

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

Response:

We agree with the structure. One suggestion is to place the Engagement Quality Management section after Acceptance and continuation.

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.

General comment

The requirements listed are in general the same as in the existing ISA:s. It is therefore difficult to see how the audit using LCE would differ from an audit where you use the existing ISA:s, specifically for the planning and risk assessment.

Our general reflection is that the requirements should be aligned with the definition of authority. The definition needs to be as clear as possible to ensure that the most complex entities are excluded. By doing this we believe that the requirements could be less detailed, for example in the planning and risk assessment section. Some of the requirements could be more generic with additional EEM.

Further general suggestions:

- The guidance to public sector is not clear. It explains that there may be a broader scope and the circumstances may look different in the public sector. While we agree with the concept of adding public sector considerations, we believe that it may be helpful to state that
 - the standard does not give any guidance on how to audit nor address these specific public sector areas
 - the guidance will have to be developed locally by each public sector audit such as a Supreme audit institution.
- We think that that the standard should more clearly open up for the possibility to scale down the amount of information the auditor needs to gather annually and work done if it is a continuous engagement. For example, the necessity to ask the management specific questions annually when you know that there have been no changes in the control environment nor the management.

Part 1 Fundamental concepts

1.3.3 – The EEM following the requirement is an indirect requirement. It describes a situation where the evaluation of audit evidence is indicating that the evidence is not sufficient. We believe that there should be a requirement stating that the auditor shall perform additional procedures to get the needed audit evidence.

1.3.4 b) – Would possibly need more clarification. Does it mean not being able to fulfill an objective because of the circumstances of the auditee (limitation in audit scope) or? The balance between achieved specific requirements and the overall objective – any reasoning on that could be helpful.

1.4.4 – Shouldn't professional judgement apply to the whole audit process and not just planning and performing?

1.6 and 1.7 – The paragraphs indicate that the auditor should not assess the risks and instead only remain alert throughout the audit. At the same time in 6.2.3 the auditor is required to assess the risk of material misstatements due to related parties. We find this being inconsistent.

Going concern is only addressed in the section on Planning and not as fundamental concept. We would suggest including it in the general concept section as well.

Part 2 Audit Evidence and Documentation

2.3 – Consider combining the EEM right after 2.3 with the EEM for 2.3.1.

2.4 – There is no requirement addressing Procedures for Obtaining Audit Evidence. There is only EEM. It is a bit unclear to the auditor what she/he is supposed to do with this information in the EEM. Would it be possible to combine the EEM with the EEMs in the 2.3 section?

2.5.1 c) – Possibly add not fulfilling any of the objectives of the LCE standard. Referring to what is stated in paragraph 1.3.4.

2.5.5. a) – Suggestion to add that the auditor should document how the management or those in charge of governance has responded to fraud issues reported just as in non-compliance issues in 2.5.5 b).

You may consider adding additional requirements on inventory, as this is not uncommon in an LCE.

Part 3 Engagement Quality Management

The concept of engagement quality control reviewer would normally not be applicable in an LCE, on our opinion. If there is a need for an engagement quality control reviewer, it implies that the audit is complex or the entity is listed. Referring to paragraph 3.2.13.

If kept within the standard our suggestion would be to shorten the section as it is overwhelming. As for example we find paragraph 3.2.11 to be a good example of a paragraph which is clear and gives room for the engagement partner professional judgement for level of engagement.

Part 4 Acceptance or Continuance

We find it a bit odd to have this section after Engagement Quality Management. We would prefer to have it before.

Consider adding more guidance on initial audit engagements or imply that new audit engagements should not be audited with LCE. It may be difficult to assess the risks appropriately in an initial audit. Therefore, it could be relevant to scope these engagements out of this standard.

Part 5 Planning

The LCE does not include any reference to the use of internal auditor work. In the public sector you may find internal auditors even in smaller and less complex entities. This is usually an effect of mandatory internal audit on the state level of governance. We would suggest some reference to what the auditor needs to consider if using the work of internal audit.

In our opinion, an audit where there is a need for an auditor's expert would not be considered an LCE. The need for an expert implies that there are complex matters that should scope the audit out of this standard. Therefore, we believe that the requirements regarding an auditor's expert could be removed from the standard.

Part 6 Risk identification and assessment

The requirements are basically the same as in ISA 315 (revised). Doing the planning and risk assessment part is crucial. Though the question is whether we would need to gather all the listed mandatory information and assess all the specifics in the understanding the internal control systems, for a less complex entity. The challenge is to tighten the standard to ensure reasonable assurance but not to overwhelm the auditor and causing an inefficient audit.

Gathering all information and understanding every part of the internal control system for the smaller and less complex entities is extremely time consuming. In general, there are

minimal changes over the years, but the suggested requirement is to annually update every part. Comparing our approach of today with the new standard would not lead to any efficiency in our work.

What we would suggest is to

- Ensure that the requirements are less detailed and more generic, followed by examples of types of information in an EEM where you list a number of information that may be relevant to gather. For example, paragraph 6.3.1 which says that the auditor shall understand specific information about the entity listed in a–f). Our suggestion would be to state that the auditor needs to understand the business and environment of the entity followed by an EEM with the information listed in a–f. The same approach would apply for paragraph 6.3.6 on control environment but highlighting that you need to do more if you aim to rely on controls (test of controls).
- Highlight the importance of professional judgement.
- Enhance that the auditor is encouraged to use information from previous years and ask for confirmation that it has not changed.
- Highlight that the auditor may need to do more if there have been significant changes at the auditee in terms of business direction, organization, change of top management etcetera. We think it is important to drive the audit work towards parts where there have been significant changes compared to the previous year and not to automatically repeat the same procedures as the previous year.
- Highlight that the auditor may use the information from the previous year written representations in the risk assessment instead of asking the same questions shortly after. Under the condition that the risk assessment/planning is done shortly after the auditor's report is presented.
- Consider combining paragraph 6.8.2 and 6.5.11.

Part 7 Responding to assessed risk of material misstatement

7.3.6 – The requirement states that the auditor should project misstatements found in the samples for the population. This is statistically not possible unless you use a statistically designed random sampling method. The question is whether there is a need to use statistically random sampling methods for an audit of a LCE.? This means that the requirements are stricter, than for a non LCE. When auditing a small, less complex entity you may also audit all transactions or just chose the transactions you find to be suspicious or high risk.

7.3.5 and 7.3.7 – It is not clear whether these paragraphs refer to test of details or sampling as a technique. Sampling may be used when selecting control activities to test. Therefore paragraph 7.3.7 is a bit unclear. It is not the result of the sample that is relevant – instead it would be whether the test of details have provided a reasonable assurance.

7.4.27 – Audit experts. If the entity is complex enough that you need an audit expert, then the auditor should probably not use this standard and the entity not be defined as LCE. Our suggestion would be to exclude this guidance and consider listing the use of audit experts as a criteria for defining LCE.

Part 8 Concluding

No comments.

10. For Part 9, do you agree with the approach taken in ED-ISA for LCE with regard to auditor reporting requirements, including:

(a) The presentation, content and completeness of Part 9.

(b) The approach to include a specified format and content of an unmodified auditor's

report as a requirement?

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

Response:

Yes, we agree with the approach taken on auditor reporting, including the presentation etc.

11. With regard to the Reporting Supplemental Guide:

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

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

Response:

Yes, it is helpful and we have not identified any additional matters that should be included.

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

Response:

No further comments. We refer to our comments above.

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?

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

Response

No comments.

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

Response:

Yes.

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

Response

Yes.

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

Response:

No comments

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.
- (b) Whether the proposed standard meets the needs of auditors, audited entities, users of audited financial statements and other stakeholders.
- (c) Whether there are aspects of the proposed standard that may create challenges for implementation (if so, how such challenges may be addressed).

Response

In general, there are no main differences between a full scope ISA audit and using LCE, if you are auditing as small less complex entity. Therefore, the answer to this question would be yes. Though we think that there is a point of going back to the original idea of the need of this standard and compare it to the draft. A couple of the initiatives were driven by cost-effectiveness, scalability etcetera. We do not think that this standard has fully fulfilled the objective of being a good solution for auditing less complex entities.

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

Response

No further comments.

Section 4G - Approach to Consultation and Finalization

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

Response

A practical example of the knowing the entity and risk assessment process would be beneficial just to see how much you need to do.

Request for Comments – General Questions

In addition to the requests for specific comments above, the IAASB is also seeking comments on the matters set out below:

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

Response

No comments

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

Response:

Agree with your suggestion.