

Meeting: IAASB Consultative Advisory Group (CAG)
Meeting Location: New York, United States of America
Meeting Date: September 12-13, 2023

Agenda Item

C

Audits of Less Complex Entities (LCE) – Cover

Objective of Agenda Item

1. The objectives of this agenda item are to:
 - (a) Report back on Representatives' comments made at the March 2023 IAASB CAG meeting.
 - (b) Receive an overview of the significant issues from comments to the Exposure Draft of Part 10 (Group Audits) of the proposed ISA for LCE.
 - (c) Obtain Representatives' views on the draft proposed ISA for LCE standard, including Part 10.

Project Status

Part 10, Audits of Group Financial Statements

2. The [Exposure Draft of the Proposed Part 10, Audits of Group Financial Statements of the Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex](#) (ED-Part 10) was published in January 2023, and the public consultation ended on May 2, 2023. Since the public consultation, the IAASB has been considering feedback from respondents in progressing the finalization of Part 10. The IAASB has discussed this project in its July 2023 meeting. Among the key matters discussed were:
 - The prohibition related to component auditors;
 - Group-specific qualitative characteristics; and
 - Content of Part 10 and conforming amendments.

Proposed ISA for LCE

3. Since the March 2023 meeting, the ISA for LCE Task Force (the Task Force) further develop the draft of the proposed ISA for LCE based on respondents' comment on the [Exposure Draft of the International Standard on Auditing for Audits of Financial Statements of Less Complex Entities](#) (ED-ISA for LCE) and input from the IAASB and IAASB CAG.
4. The Task Force presented to the IAASB a full draft of the proposed ISA for LCE, except for Part 10 to the Board in June 2023. Part 10 was presented to the Board in July 2023.
5. In developing the current draft of the proposed ISA for LCE (as presented in **Agenda Item C.2**), the Task Force liaised with:
 - Other IAASB Task Forces and Working Group, including the:
 - Complexity, Understandability, Scalability and Proportionality Working Group;

- Professional Skepticism Working Group;
 - Technology Working Group; and
 - Auditor Reporting Working Group.
- International Ethics Standards Board for Accountants' (IESBA)
6. The **Appendix** to this paper provides a history of previous discussions with the IAASB CAG and IAASB on this topic, including links to the relevant IAASB CAG documentation.

Way Forward

7. The Task Force is planning to obtain approval of the ISA for LCE at the September 2023 IAASB meeting.
8. After the September 2023 meeting, the Task Force will focus on:
- Further revisions to the Supplemental guides on Authority and Reporting based on feedback received;
 - Developing supplemental guidance on implementation and transition; and
 - Liaising with the International Federation of Accountants and other key stakeholders on the adoption of the standard.

IAASB CAG Discussion in September 2023

9. For purposes of the IAASB CAG discussion, the Task Force Chair will walk the Representatives through a presentation (**Agenda Item C.1**), that summarizes some of the key revisions the Task Force has proposed to proposed ISA for LCE (as presented in **Agenda Item C.2.**) since the March 2023 CAG meeting.
10. In addition to the matters in this Agenda Item and **Agenda Item C.1.**, **Agenda Item C.2.**, representatives are encouraged to read the following sections in **Agenda Item C.6**:
- Section III, Question 21 – Effective Date
 - Section III, Question 14 – Maintenance
 - Section III, Question 19 – Implementation Guidance

Matters for IAASB CAG Consideration

1. The Representatives are asked for their views on the proposed ISA for LCE as presented in **Agenda Item C.2**:
- (a) Preface and Authority;
 - (b) Parts 1–5; and
 - (c) Parts 6–10.
2. Representatives are asked for their views on:
- (a) The effective date of ISA for LCE;
 - (b) The maintenance of the ISA for LCE; and

- (c) The IAASB’s plan on adoption and Implementation.
3. Representatives are asked whether there are any other matters that the LCE Task Force should consider as it finalizes proposed ISA for LCE.

Report Back

11. Extracts from the draft minutes of the March 2023 IAASB CAG meeting, as well as an indication of how the Task Force or IAASB has responded to the Representatives’ comments, are included in the table below.

Representatives’ Comments	Task Force / IAASB Response
PROPOSED REVISIONS TO PARTS 2-5	
Drs. Manabat, Cela and Norberg, Mr. Thompson, and Ms. Blomme supported the direction of revisions in Parts 2-5. Ms. Blomme also supported the project overall.	Support noted. Mr. Hagen thanked Representatives for their comments and noted that documentation is a tricky area to find the right balance, not only for the ISA for LCE but for the ISAs as well.
Ms. Blomme suggested clarifying that when a requirement is not applicable, the auditor is not required to document why.	Point not accepted. Mr. Hagen noted the LCE Task Force considered adding this but did not include it as it was not deemed necessary and there were concerns that it may not drive the right behavior.
Ms. Mubarak noted the importance of including a key principle of ISA 230 that the auditor shall prepare audit documentation that is sufficient to enable an experienced auditor having no previous connection with the audit to understand the conclusions reached.	Point accepted. Mr. Hagen noted that the principle is included in Part 2 of the ISA for LCE.
Mr. Yurdakul noted concern regarding allowing too much professional judgment relating to documentation. He agreed with defining clear guidelines to ensure sufficient documentation. Dr. Norberg added that documentation is tricky to address, but is important.	Point noted. Mr. Hagen explained that based on the feedback on the ED-ISA for LCE there are different views around this area but by including both general and specific documentation requirements, concerns should be addressed. The proposed ISA for LCE follows the same approach as the ISAs by including general document requirements outlining key principles, and specific documentation requirements as relevant to the content included in each part.

Representatives' Comments	Task Force / IAASB Response
<p>Dr. Norberg noted that the engagement letter is used by clients to understand “what they are paying for” and what standard is applied and suggested that the engagement letter should indicate the standard intended to be used. Mr. Fritz agreed.</p>	<p>Point accepted.</p> <p>Mr. Hagen explained that the ISAs do not have a similar requirement, and that both an audit using the ISAs and the ISA for LCE should result in reasonable assurance. He also noted that jurisdictions can add such a requirement.</p> <p>In the March 2023 IAASB meeting it was decided to add back the requirement to record in an engagement letter, or other suitable form of written agreement, that the audit will be undertaken using the ISA for LCE. The IAASB was of the view that it is important to be transparent to management which auditing standards are used and that this is aligned with what is disclosed in the auditor’s report.</p>
<p>PROPOSED REVISIONS TO PART 6</p>	
<p>Dr. Norberg and Ms. Blomme supported the revisions proposed to make Part 6 more proportionate to LCEs. Dr. Norberg noted that in a typical LCE, management and the owner will often be the same person, and that Part 6 is proportionate to these circumstances.</p>	<p>Support noted.</p>
<p>Ms. Wolf questioned if there would be a stand back included in Part 6, for the auditor to consider if the ISA for LCE is still relevant after risk identification and assessment is performed. Dr. Norberg agreed, noting that it is critical to find the right balance in determining which requirements from the ISAs will be included in Part 6 and which not. Mr. Sobel questioned if the ISA for LCE covers the situation where an LCE becomes a non-LCE since risks can change as an audit progresses.</p>	<p>Points noted.</p> <p>Mr. Hagen clarified that there are requirements for the auditor to consider if the entity is still an LCE throughout the audit. Mr. Hagen noted that if the entity is no longer an LCE (e.g., the auditor changes or enters into complex transactions) then the auditor has to transition to another standard. He noted that given that the Authority gives better direction on what the typical LCE is, it should also be easier for the auditors to decide if they are using the right standard or not.</p> <p>Mr. Botha added that the Task Force has worked on making clearer the group of entities in the spectrum of complexity that the ISA for LCE is targeting so that when auditors apply the Authority the auditors are more likely to “get it right”. Mr. Botha noted there may still be a</p>

Representatives' Comments	Task Force / IAASB Response
	<p>chance that the auditor will have to go back to the ISAs, but in that case, they can “take credit” for the work performed so far. Mr. Botha clarified that the Task Force has not yet discussed with the Board the detailed respondent comments regarding transition.</p>
<p>Mr. Ruthman noted that some of the public sector considerations in ISAs are not reflected in the ISA for LCE and encouraged the LCE Task Force to include more public sector specific considerations and include guidance that explains that there are additional public sector related considerations in the ISAs.</p>	<p>Point noted.</p> <p>Mr. Hagen noted that the LCE Task Force is still working through public sector considerations and will consider Mr. Ruthman’s comments. He also explained that the ISA for LCE is designed to be a stand-alone standard so there will not be direct references to ISAs but the relevant content will be included.</p> <p>Mr. Ruthman’s comments, along with comments from respondents to ED-ISA for LCE specifically relating to the public sector, were considered when make revisions to the revised standard. This included considering the need for additional EEM, or revisions to existing EEM relating to specifically to public sector entities.</p>
<p>Mses. McGeachy and Blomme noted that the auditor should not be required to test the design and implementation of controls when the auditor is not intending to rely on the controls.</p>	<p>Point noted.</p> <p>Mr. Hagen acknowledged that similar concerns have been raised by stakeholders and Messrs. Hagen and Botha explained that it is important for understanding the entity, for identifying risk of material misstatement and that it helps in planning the audit. Mr. Botha added that the testing of design and implementation of controls is only required for certain control activities and it is not that onerous.</p>
<p>Mr. Hansen inquired about how the ISA for LCE addressed the performance of risk assessments, as some stakeholders want to address control risks and inherent risks together and some want them to be addressed separately.</p>	<p>Point noted.</p> <p>Mr. Botha explained that in ISA 315 (Revised 2019)¹ the assessment of control risk and inherent risk are separated. In addition, for inherent risk, the auditor identifies the risks of material misstatements and then assesses them. For the ISA for LCE, to be proportionate</p>

¹ ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

Representatives' Comments	Task Force / IAASB Response
	<p>to LCEs, the identification and assessment of inherent risk are combined and when the auditor is not relying on internal control the risk of material misstatement is equal to the inherent risk.</p> <p>Mr. Hagen noted that the requirement to consider and document against the set list of inherent risk factors has been removed but is now included in guidance on what to consider when assessing inherent risks, in order to reach the same outcome.</p>
<p>Mr. Ruthman questioned the terminology used in the essential explanatory material under paragraph 6.4.3E noting that “contemplate” is not as firm as “intention” when referring to the auditors’ intention to rely on controls.</p>	<p>Point not accepted.</p> <p>Mr. Hagen explained that this wording is consistent with Paragraphs 6 and A71 of ISA 315 (Revised 2019).</p>
<p>Ms. McGeachy noted that the work effort verb of “consider” is more appropriate than “evaluate” for paragraph 6.3.6., for a typical LCE.</p>	<p>Point not accepted.</p> <p>The wording is consistent with Paragraph 21 of ISA 315 (Revised 2019).</p>
PROPOSED REVISIONS TO ACCOUNTING ESTIMATES	
<p>Mr. Dalkin questioned if an accounting estimate that involves an actuary would be considered complex. Mr. Hansen added that the same question could be asked regarding the use of experts more generally. Ms. Wolf noted that she would not have concern if the ISA for LCE is permitted to be used when there is an accounting estimate (e.g., a pension reserve) and an expert to whom the auditor has access to is used for the audit procedures and the entity is still an LCE.</p>	<p>Point noted.</p> <p>Mr. Hagen explained that the LCE Task Force did discuss such examples and noted that it depends on the facts and circumstances whether an accounting estimate is complex.</p>
<p>Dr. Norberg supported the direction. He noted that accounting standards could require complex measurement that do not reflect the complexity of the entity. Dr. Norberg added his support on the revisions to requirements and the Authority, noting the distinction between the accounting of an accounting estimate and complexity of an entity.</p>	<p>Support noted.</p>

Representatives' Comments	Task Force / IAASB Response
<p>Ms. Gamboa questioned whether there was intention to include examples or guidance on what will constitute complex methods or model and to help auditors interpret the word “typically” in the qualitative characteristic.</p>	<p>Point noted.</p> <p>Mr. Hagen noted the intention for supplemental guidance to help understand if engagements are in the scope or not.</p> <p>Guidance on this matter will be included in the Supplemental Guide on Authority which is currently in development.</p>
OTHER COMMENTS	
<p>Ms. McGeachy noted that there is a risk that the quantitative thresholds proposed to be included in the Authority will become “de facto” what a jurisdiction will use. She added that since only small sized entities are used as examples, medium sized entities may not be permitted to use the standard.</p>	<p>Point noted.</p> <p>Mr. Hagen explained that the examples are trying to signal what type of engagements the IAASB considered when the standard was developed, and it is something that the jurisdiction need to consider when they evaluate or consider the use of the ISA for LCE and adjust for jurisdictional differences. Mr. Hagen added that whether the examples provided become de facto is up to the standard setters or regulators in the jurisdictions.</p> <p>Guidance on this matter be included in the Supplemental Guide on Authority which is currently in development.</p>
<p>Ms. Blomme and Dr. Cela applauded the release of ED-Part 10. Ms. Blomme noted that the exclusion of component auditors may be too restrictive. Mr. Thompson noted that they will respond to ED-Part 10 and may suggest broadening the scope.</p>	<p>Support noted.</p> <p>Respondents to ED-Part 10 had mixed views on whether there should be a prohibition on the use of component auditors. Based on these mixed views and previous discussion on the authority of the ISA for LCE, the Board agreed that the prohibition to use component auditors (with the exception of when the component auditor’s involvement is limited to circumstances in which a physical presence is needed for a specific audit procedure for the group audit) is the best way forward.</p>

Representatives' Comments	Task Force / IAASB Response
<p>Mr. Ishiwata noted that component auditors are not prohibited from using ISA for LCE for the purposes of the group or statutory audit. He questioned whether they should be prohibited from the use of the ISA for LCE to assure a high-quality audit.</p>	<p>Point not accepted.</p> <p>Mr. Hagen noted that under ISA 600 (Revised)² the group auditor decides which auditing standards should be used for purposes of the group audit and that the component auditor needs to comply with those auditing standards. The component auditor may decide to use different auditing standards for a statutory audit.</p>
<p>Dr. Cela noted that EFAA and the IAASB organized a webinar to update stakeholders on the project. Mr. Thompson added that there is significant global interest in the project given the number of participants and the geographical representation of the participants. He also noted that the project is in the public interest and would foster greater trust and confidence in SMEs' financial statements and helps to build the accountancy profession in the emerging and transitional markets.</p>	<p>Point noted.</p>
<p>Mr. Ishiwata noted that IAASB is undertaking several important projects such as sustainability assurance, going concern and fraud and noted that IAASB's resources should be allocated to these projects given that these projects have a broader impact.</p>	<p>Point not accepted.</p> <p>Mr. Seidenstein explained that the resources used to develop the ISA for LCE are not diverting any resources from any other major public interest projects. He added that it is in the public interest to serve this group of stakeholders and that he believes that the IAASB's views are aligned with PIOB's.</p>

² ISA 600 (Revised), *Special considerations - Audits of Group Financial Statements (Including the Work of Component Auditors)*

Representatives' Comments	Task Force / IAASB Response
<p>Mr. Hansen asked if audits of pension schemes and collective investment vehicles which were not included in the final Public Interest Entity (PIE) definition revised by IESBA, are excluded from the scope of ISA for LCE.</p>	<p>Point noted.</p> <p>Mr. Hagen explained that the LCE Task Force is considering further revisions to align with the PIE project.</p> <p>In the Authority, the classes of entities in paragraph A.1.(c) are aligned with the classes in the final revised IESBA Revisions to the <i>Definitions of Listed Entity and Public Interest Entity in the International Code of Ethics for Professional Accountants (including International Independence Standards)</i> (the IESBA Code). The definition of a PIE in the IESBA Code serves a different purpose than the description of classes of entities that may exhibit public interest characteristics that would make the use of the ISA for LCE inappropriate, respondents to the ED-ISA for LCE expressed the importance of aligning them to the greatest extent possible to avoid confusion.</p>
<p>Mr. Dalkin questioned whether there are any coordination efforts with the IESBA.</p>	<p>Point noted.</p> <p>Mr. Hagen noted that the project team regularly coordinates with IESBA on matters of relevance.</p>

Material Presented – IAASB CAG Papers

Agenda Item C.1: Presentation

Agenda Item C.2: Proposed ISA for LCE

Material Presented – IAASB CAG Reference Papers

Agenda Item C.3: ISA for LCE Conforming Amendments (For Reference)

Agenda Item C.4: IAASB Issues Paper (June 2023) (For Reference)

Agenda Item C.5: IAASB Issues Paper (July 2023) (For Reference)

Agenda Item C.6: IAASB Issues Paper (September 2023) (For Reference)

Project Details and History

Project: Audits of Less Complex Entities

Link to IAASB Focus Area Page: [ISA for LCE Focus Area Page](#)

Link to IAASB Project Page: [Audits of Less Complex Entities Project Page](#)

Task Force Members

- Kai Morten Hagen, IAASB Member and Task Force Chair
- Julie Corden, IAASB Member
- Chun Wee Chiew, IAASB Member
- Sachiko Kai, IAASB Member
- Vivienne Bauer, IAASB Technical Advisor

Summary

	IAASB CAG Meeting	IAASB Meeting
Information Gathering	March 2017 September 2017 September 2018 March 2019 March 2020 September 2020	March 2017 March 2018 (Executive session) September 2018 March 2019 December 2019 April 2020 June 2020
Project Proposal	December 2020	December 2020
Development of Exposure Draft of ISA for LCE	March 2021 September 2021	March 2021 May 2021 June 2021
Development of final ISA for LCE	September 2022 March 2023	June 2022 September 2022 December 2022 March 2023

	June 2023 July 2023
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IAASB CAG Discussions: Detailed References

Information Gathering	<p><u>March 2017</u> See IAASB CAG meeting material (Agenda Item G).</p> <p><u>September 2017</u> See IAASB CAG meeting material (Agenda Item C).</p> <p><u>September 2018</u> See IAASB CAG meeting material (Agenda Item I).</p> <p><u>March 2019</u> See IAASB CAG meeting material (Agenda Item E).</p> <p><u>March 2020</u> See IAASB CAG meeting material and CAG (Agenda Item N).</p> <p><u>September 2020</u> See IAASB CAG meeting material (Agenda Item E).</p>
Project Proposal	<p><u>December 2020</u> See IAASB CAG meeting material (Agenda Item A).</p>
Development of Exposure Draft of ISA for LCE	<p><u>March 2021</u> See IAASB CAG meeting material (Agenda Item D).</p> <p><u>September 2021</u> See IAASB CAG meeting material (Agenda Item F).</p>
Development of final ISA for LCE	<p><u>September 2022</u> See IAASB CAG meeting material (Agenda Item B).</p> <p><u>March 2023</u> See IAASB CAG meeting material (Agenda Item G).</p>