

October 4, 2022

IFAC Small and Medium Practices Advisory Group Response to the IAASB's Exposure Draft proposed *Narrow Scope Amendments to ISA 700 (Revised) and ISA 260 (Revised) as a Result of the Revisions to the IESBA Code that Require a Firm to Publicly Disclose When a Firm Has Applied the Independence Requirements for Public Interest Entities (PIEs)*

INTRODUCTION

The IFAC SMP Advisory Group (SMPAG) is pleased to respond to the IAASB (the Board) Exposure Draft (ED), proposed *Narrow Scope Amendments to ISA 700 (Revised), Forming an Opinion and Reporting on Financial Statements, and ISA 260 (Revised), Communication with Those Charged with Governance, as a Result of the Revisions to the IESBA Code that Require a Firm to Publicly Disclose When a Firm Has Applied the Independence Requirements for Public Interest Entities (PIEs)*.

The SMPAG is charged with identifying and representing the needs of its constituents and, where applicable, to consider relevant issues pertaining to small- and medium-sized entities (SMEs). The constituents of the SMPAG are small- and medium-sized practices (SMPs) who provide accounting, auditing, assurance, and business advisory services principally, but not exclusively, to clients who are SMEs. Members and Technical Advisers serving the SMPAG are drawn from IFAC member organizations representing 22 countries from all regions of the world

GENERAL COMMENTS

The SMPAG supports the IAASB approach to undertake the project on listed entity and PIE as two tracks with the ED focused on narrow scope amendments to ISA 700 (Revised) and ISA 260 (Revised) to support operationalizing the IESBA transparency requirement with an effective date that aligns with the revisions to the IESBA Code, followed by a separate track dealing with other issues that would have a later effective date.

The SMPAG supports the IAASB's proposed approach to have a conditional requirement in paragraph 28 (c) of ISA 700 (Revised) that applies only when the relevant ethical requirements require public disclosure that differential independence requirements for audits of financial statements of certain entities were applied. In our view, this is a pragmatic solution to implementing the requirement of the IESBA Code (R400.20) in a manner deemed appropriate. We also agree with the revisions to ISA 260 (Revised) to increase transparency to those charged with governance that differential independence requirements for certain entities have been applied.

Below are our detailed comments related to the questions in the ED.

DETAILED COMMENTS

Transparency About the Relevant Ethical Requirements for Independence for Certain Entities Applied in Performing Audits of Financial Statements

1. Do you agree that the auditor's report is an appropriate mechanism for publicly disclosing when the auditor has applied relevant ethical requirements for independence for certain entities in

performing the audit of financial statements, such as the independence requirements for PIEs in the IESBA Code?

The SMPAG agrees that the auditor's report is an appropriate mechanism for publicly disclosing when the auditor has applied relevant ethical requirements for independence for certain entities in performing the audit of financial statements, such as the independence requirements for PIEs in the IESBA Code.

2A. If you agree:

(a) Do you support the IAASB's proposed revisions in the ED to ISA 700 (Revised), in particular the conditional requirement as explained in paragraphs 18-24 of the Explanatory Memorandum?

(b) Do you support the IAASB's proposed revisions in the ED to ISA 260 (Revised)? 2B. If you do not agree, what other mechanism(s) should be used for publicly disclosing when a firm has applied the independence requirements for PIEs as required by paragraph R400.20 of the IESBA Code?

The SMPAG submitted a [comment letter](#) in response to the IESBA Exposure Draft *Proposed Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code*. The letter expressed concerns about the proposal for firms to disclose if they treated an audit client as a PIE for auditor independence purposes because of the likely implications and potential unintended consequences.

The main SMPAG concern was about the risk that it may add to the expectation gap in auditing. It is also raised the risk that further misunderstanding, and confusion could occur, especially if the disclosure is that the entity is treated as a PIE, despite that entity being excluded from legal/regulatory PIE definitions in a particular jurisdiction. Disclosing such information may also require disclosing what it means i.e., the firm would need to also explain why they chose a particular entity to be considered a PIE from their perspective and describe what ways the audit undertaken differed from an audit of a non-PIE.

In addition, the letter raised that greater confusion in the market could ensue where firms offer different explanations and descriptions of why they have treated client entities as PIEs, and it could also be perceived as an attempt to be a "gold seal of approval" for an audit firm or an audit client. In our view, taking all of this into account means that what might, on the face of it, seem to be a very simple disclosure becomes very detailed and complex. As a result, it raises multiple questions about the value of the disclosure from a cost-benefit perspective.

The comment letter did note that were IESBA and IAASB to pursue this issue further, the auditor's report did seem to be the most appropriate place for such a disclosure. As the decision about treating an entity as a PIE is, in such cases, being made solely by the auditor, then the auditor's report is the only communication that is owned by the auditor. The disclosure would need to be in that communication; it could not be in the entity's own communications.

The SMPAG supports the IAASB approach to include a conditional requirement that applies only when the relevant ethical requirements require public disclosure that differential independence requirements for audits of financial statements of certain entities were applied. This approach addresses the concerns we had raised in our letter to IESBA outlined above, since only when the condition is met, is the auditor required

to indicate in the auditor's report that the relevant ethical requirements for independence for those entities were applied.

The SMPAG also generally supports the proposed revisions in the ED to ISA 260 (Revised) because it is appropriate for those charged with governance to be made aware that differential independence requirements for certain entities have been applied. However, we did receive a concern on the use of the word 'differential' so the Board could consider if this could be deleted while still retaining the same intended message.

Transparency About the Relevant Ethical Requirements for Independence for Certain Entities Applied in Performing Reviews of Financial Statements

3. Should the IAASB consider a revision to ISRE 2400 (Revised) to address transparency about the relevant ethical requirements for independence applied for certain entities, such as the independence requirements for PIEs in the IESBA Code?

4. If the IAASB were to amend ISRE 2400 (Revised) to address transparency about the relevant ethical requirements for independence applied for certain entities, do you support using an approach that is consistent with ISA 700 (Revised) as explained in Section 2-C?

Notwithstanding that SMPs may be engaged to perform audits of the financial statements of PIEs, we believe that (even for non-SMPs) engagements to perform reviews of financial statements are exceedingly rare for public interest entities, so ISRE 2400 (Revised) is rarely applicable.

However, if despite this, the IAASB did decide to make conforming amendments to ISRE 2400 (Revised) to address transparency about the relevant ethical requirements for independence applied for certain entities, the SMPAG would support using an approach that is consistent with ISA 700 (Revised).

In addition, we also suggest consideration of a revision to ISRE 2410 (Revised) using the approach that is consistent with ISA 700 (Revised) as this standard is commonly used for listed entity interim review engagements.

General Comments

5. Translations—Recognizing that many respondents may intend to translate the final pronouncement for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents note in reviewing this ED.

We did not identify any specific translation issues in reviewing this ED.

However, we would like to take the opportunity to make the IAASB aware that we continue to hear significant challenges from both member organizations and SMPs about keeping up with the pace of change in international standards, in particular with translations. This has been heightened with the pandemic and

coupled with the economic challenges in some regions with inflation and rising interest rates, has placed an increased burden on SMPs who are trying to support and service their clients.

6. Effective Date—Given the need to align the effective date with IESBA, do you support the proposal that the amendments to ISA 700 (Revised) and ISA 260 (Revised) become effective for audits of financial statements for periods beginning on or after December 15, 2024, as explained in paragraph 26?

The SMPAG supports the proposal that the amendments to ISA 700 (Revised) and ISA 260 (Revised) become effective for audits of financial statements for periods beginning on or after December 15, 2024, to align with the effective date with IESBA.

CONCLUDING COMMENTS

We hope that the IAASB finds this letter useful. We are committed to helping the Board in whatever way we can to build upon the results of the ED.

Please do not hesitate to contact me should you wish to discuss matters raised in this submission.

Sincerely,



Monica Foerster

Chair, IFAC SMP Advisory Group