

OPTIONAL RESPONSE TEMPLATE: PROPOSED ISA FOR LCE

Guide for Respondents

- The International Auditing and Assurance Standards Board (IAASB) has published this separate Microsoft Word document for respondents to use for submitting their comments, if they wish. The questions below are from the exposure draft of proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities Management (ED-ISA for LCE), which is available at www.iaasb.org/publications/exposure-draft-proposed-international-standard-auditing-financial-statements-less-complex-entities.
- Respondents are asked to comment on the clarity, understandability and practicality of application of ED-ISA for LCE. In this regard, comments will be most helpful if specific aspects of ED-ISA for LCE are identified and the reasons for any concerns along with suggestions for improvement, are included. Specific suggestions for any proposed changes to wording in ED-ISA for LCE are also welcome.
- **Respondents are free to address only questions relevant to them, or all questions.** When a respondent agrees with the proposals in ED-ISA for LCE, it will be helpful for the IAASB to be made aware of this view as support for the IAASB’s proposals cannot always be inferred when not explicitly stated.
- We request that comment letters do not include tables as they are incompatible with the software we use to help analyze respondents’ comments.

Comments are requested by January 31, 2022

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| Name of Respondent: | <u>Claes Norberg</u> |
| Organization (<i>where relevant</i>): | <u>Confederation of Swedish Enterprise</u> |
| Country/Region/Jurisdiction: | <u>Sweden</u> |

General Comments on Proposed ISA for LCE

The Confederation of Swedish Enterprise welcomes the proposal on ISA for LCE. We support the overall approach, i.e. that the standard can be applied as an option if the criteria for applying it are satisfied. We consider that there are three conditions that must be met in order to achieve the objectives of the proposed standard (to enhance confidence of intended users in the financial statements of the entity).

- 1. Trust from stakeholders that the objectives will be achieved. Otherwise, there is a great risk that the standard will not be applied and full ISA will be applied instead. Resistance and/or lack of understanding or knowledge about ISA for LCE increases the risk of non-application.*
- 2. That the scope of application is drafted in such a way that it is operational for e.g. auditors, regulators, standard-setters and stakeholders.*
- 3. That the content of the ISA is sufficient and relevant so that an auditor can issue a reasonable assurance opinion.*

Good drafting of the standard is of course vital to achieve the objectives. To ensure that the standard is accepted and operational we believe that the IAASB should engage in further outreach to users of financial information and other stakeholders and field-test the draft standard before it is adopted.

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?

Response: We support the approach of a separate standalone standard. We believe that the application of the standard should result in a reasonable assurance opinion and that this opinion shall be in the form of an audit opinion. Any other level of assurance would signal that applying ISA for LCE does not result in a “full” audit.
 - (b) The title of the proposed standard.

Response: We support to name the standard ISA for LCE.
 - (c) Any other matters related to ED-ISA for LCE as discussed in this section (Section 4A).

Response: N/A
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: We agree.

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?

Response: We do support that there are specific prohibitions in the Authority. We do not support that decisions about the application of the standard are taken at the audit firm or engagement level. We believe that that decisions on when the standard may be applied should be taken at jurisdictional level (by law, or by regulators and/or standard-setters).

We believe that the qualitative characteristics should be used by regulators and standard-setters when deciding which entities should be scoped out, apart from specific prohibitions and jurisdictional level limitations.

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

Response: We believe that one consequence of letting firm policies or procedures decide if ISA for LCE should be applied or not is that it might have an impact on international/global level. If a global audit firm prohibits the use of ISA for LCE generally, for whatever reason, this might have a huge impact on the application of the standard.

Further, if audit firms apply different policies regarding the use of ISA for LCE in a specific jurisdiction this might also lead to confusion. Differences in the application of audit standards might be that difficult to understand for stakeholders. If such consequences are unintended or not can be debated.

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

Response: We believe that areas described are sufficiently clear. It is also accepted that judgement is needed when interpreting the Authority. It is not a matter of clarity. Instead, we consider that complexity, especially when assessing the qualitative characteristics, is the main concern when applying the Authority. Please also see our response to question (d) below.

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

Response: We believe that the specific prohibitions and jurisdictional level limitations are sufficiently clear. There might be bigger challenges for stakeholders to understand firm policies and procedures and engagement level evaluation. Especially the engagement level is challenging since this requires knowledge and understanding of the qualitative characteristics. We are concerned that a complex assessment of a number of different facts and circumstances is needed, which might be difficult for the auditor. We also are concerned that stakeholders might not fully understand the qualitative characteristics and how they are interpreted and applied.

(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: Yes, we agree. We consider that when applying the Authority at jurisdictional level it may for practical reasons be necessary to also consider size of the audit client. We support using thresholds at jurisdictional level.

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

Response: We strongly disagree with the exclusion of audits of group financial statements. We consider that the argument presented for the prohibition (that group audits inherently exhibit characteristics of complexity within an entity) is not convincing. We believe that the consolidation process to draw up group financial statements is very basic and well understood by auditors. We acknowledge that audits of business combinations, intra-group transactions etc do involve a number of issues to address for the auditor, but we think that this in itself should not scope out audits of group financial statements.

Scoping out audits of group financial statements would limit the scope of application too much. Many small or micro entities without complex qualitative characteristics do belong to groups. One example is that entities in a jurisdiction might have a real estate in a subsidiary (as the lone asset). If the real estate would have been on the balance sheet of a single entity and the entity would have passed the ISA for LCE test regarding complexity, then the standard could have been applied. It then seems reasonable that a group audit in this case should not be scoped out.

We consider that instead of excluding audits of group financial statements from ISA for LCE, there should be a test to assess whether the entities in the group can be considered to be less complex entities. If all entities within the group pass this test, then also the group financial statements should be possible to audit applying ISA for LCE.

(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: We have some comments on the entity's accounting estimates. According to A.9. in the draft standard, that the entity's accounting estimates are subject to a higher degree of estimation uncertainty or that the measurement basis requires complex methods that way involve multiple sources of historical and forward-looking data or assumptions, with multiple relationships between them, is an indication that it is inappropriate to apply the ISA for LCE. In the Draft Supplemental Guidance a number of examples of accounting complexity is described.

We believe that starting point, i.e. estimation uncertainty, needs to be put into a perspective. There are very few assets that have reliable and observable market prices. Most assets and liabilities in a balance sheet are measured using a measurement technique, in accordance with the applicable accounting standard for the entity. This means that in most cases there will be some degree of measurement uncertainty present. Uncertainties will be resolved when the asset is sold or consumed or the liability is extinguished. We therefore think that it is somewhat difficult to assess "when there is a higher degree of estimation uncertainty or that the measurement basis requires complex methods that way involve multiple sources of historical and forward-looking data or assumptions". None of these features are defined in the draft standard and in order to assess when such a complexity is present, some type of "baseline" needs to be established.

We appreciate the examples in Draft Supplemental Guidance, but we think that there is a lack of a holistic view. In the examples, fair value accounting using Level 1 inputs passes as non-complex while fair value accounting using Level 3 inputs is deemed to be complex. Examples relating to a specific asset or a liability are of limited help when assessing the accounting policies of an entity. Should fair value accounting of a portfolio of financial instruments using Level 3 inputs lead to a

classification of the accounting as complex if all other assets and liabilities are valued at historical cost in an entity? And should that have an impact on which auditing standard that should be applied?

We believe that an alternative is to assess the applicable accounting standards for the entity instead of focusing on the accounting of a specific item. This means that local GAAP might have an impact on the assessment of complexity. If the entity e.g. applies an accounting standard specially designed for SMEs, this could be an indication that the accounting is less complex.

5. Regarding the Authority Supplemental Guide:

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

Response: We believe it is helpful in general.

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

Response: N/A

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: N/A

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).*

Response: We believe the chosen approach is appropriate.

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

Response: We support the chosen approach.

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

Response: We support the chosen approach.

(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.*

Response: We support the chosen approach.

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).

Response: We support the chosen approach.

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.

Response: N/A.

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: We support the chosen approach.

11. With regard to the Reporting Supplemental Guide:

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

Response: Yes

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

Response: N/A

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: N/A

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?

Response: Not that we have identified.

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

Response: N/A

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

Response: Yes, we agree.

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

Response: Yes, as a principle.

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

Response: Not an urgent issue now. Can be considered later.

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.

Response: It can be used in Sweden from a legal point of view (as part of what is generally accepted auditing standards in Sweden). If will be used is not known. This is dependent on the position of the supervisory authority (the Swedish Inspectorate of Auditors). And its position is not known.

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

Response: We answer the question from an entity (audit client perspective). We believe that the standard will be beneficial for entities that will be within the scope of application. We think the application might avoid irrelevant documentation requirements from auditors and avoid future complexity coming from applying full ISA.

From a user perspective, we believe it will be sufficient for banks and the tax authority (the two main stakeholders of LCEs), if they understand the scope of the standard and how it is applied compared to full ISA.

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

Response: We have already addressed those challenges in answering question in Section 4B 4 (a) and (b).

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: N/A

Section 4G - Approach to Consultation and Finalization

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

Response: N/A

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: N/A

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: N/A

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.

Response: Please see our answer to question Section 4B 4 (a).

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?

Response: N/A

- (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?

Response: N/A

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

Response: N/A

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.

Response: The two approaches each have different benefits and weaknesses as explained in the ED. On balance, we would prefer option 1 since it is easier to apply and seems to bring more certainty to the assessment of whether the standard can be applied or not. There might also be a cost-benefit issue from an audit client perspective. Applying option 1 might be more effective.

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?

Response: As we stated in our answer to question Section 4B 4 (a), we consider that all entities in the group should be assessed to be less complex entities if audit of group financial statements is to be permitted.

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.

Response: We do not have a strong view on this.