

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

Name of Respondent:

Emilio Álvarez Pérez-Bedia

Organization (*where relevant*):

REA Auditores (Consejo General de Economistas de España-CGE)

Country/Region/Jurisdiction:

Spain

General Comments on Proposed ISA for LCE

Response: [Please include here comments of a general nature and matters not covered by the questions below.]

- We strongly support this project. The standard has the potential to drive standardization and consistency of SME audits across Europe and it may aid users understanding as to what the SME audit provides.
- Overall, we agree with the fundamental principles, design, and content of the standard. We especially like the way it follows the logical flow of the audit and the clarity and concise writing.
- We think that is vital that the communications and educational activities of the international organisations (IAASB, IFAC, PAOs...), national regulators, accounting firms and others on and around the new standard consistently and robustly stress that use of this standard results in an audit of equivalent quality to an audit performed using the ISAs.
- We have some reservations as to Authority:
 - the audit of group financial statements ought to be scoped in – many groups are less complex and, furthermore, if groups are scoped out then many LCEs that are part of a group may be required to conduct audits in accordance with full ISAs; and, in addition
 - the LCE concept with its qualitative criteria will be difficult to implement and result in inconsistent application – we prefer for size criteria to have more prominence.
- While we support the project, we urge the IAASB to simultaneously reengineer the ISAs to make them scalable from the bottom up using a 'Think Small First' approach. Accordingly, we welcome the Complexity, Understandability, Scalability and Proportionality (CUSP) project though believe it lacks ambition. Also, we would like to propose that in future revisions of the ISAs an effort be made to adjust their wording so that it is as clear and concise as the text of the LCE standard
- There is an urgent need for more support and guidance. We recognize the huge training and education effort needed for the effective implementation of the standard. We therefore encourage the Board to collaborate with IFAC in developing appropriate support and guidance. We urge IFAC to develop a Guide to the Use of ISA for LCEs.

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 agree with the standalone nature of the proposed standard.

In cases where the LCE standard does not specifically address a transaction, other event, or condition we wonder whether the auditor may use their judgment to decide how best to proceed and, in making this judgment, whether the auditor may also consider the requirements and guidance in the full ISAs

dealing with similar and related issues. This is permitted under IFRS for SMEs. Similarly, we wonder whether auditors using the LCE standard will be allowed to use full ISA requirements or application material in case they wish to voluntarily perform additional audit procedures.

(b) The title of the proposed standard.

Response:

The proposed title is appropriate. Nevertheless, if the main criteria for the determination as to scope ends up being size then we suggest: International Standard on Auditing (ISA) for Audits of Financial Statements of Small and Medium-sized Entities ('ISA for SMEs') in much the same way we have IFRS for SMEs

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

Response:

We want to state once again that is vital that the communications by the IAASB, professional accountancy organizations (PAOs), regulators, accounting firms and other on and around the new standard consistently and robustly stress that use of this standard results in an audit of equivalent quality to an audit performed using the ISAs.

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 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?

Response:

We believe that the Authority as presented is implementable in general terms. However, we have some concerns and doubts as to whether the proposed limitations relating to qualitative criteria are implementable. (see our response to Q4),

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

Response:

We are not aware of any unintended consequences that could arise.

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

Response: We believe the Authority to be clear but, as we explain in our response to Q2 and Q4, it can be difficult to implement in the case of the qualitative criteria.

(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 the Authority achieves the intended objective of appropriately informing stakeholders about the scoping of the proposed standard. The diagram in paragraph 50 and paragraphs A.5. – A.9. in ED-ISA for LCE, is logical and informative to the dedicated reader.

- (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 the proposed role of legislative or regulatory authorities or relevant local bodies with standard setting authority in individual jurisdictions to be clear and appropriate. In the European Union ('EU') the Directives are the highest source of authority.

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:

We agree with the proposed limitations relating to the use of the ED-ISA for LCEs except as explained below:

Specific prohibitions – we agree with these except for the exclusion of audits of group financial statements. Groups are not necessarily more complex than individual entities. This is especially the case when the management and ownership are concentrated in the hands of very few people: such groups tend to be managed as a single entity. Furthermore, if groups are scoped out then many LCEs that are part of a group may be required to conduct audits in accordance with full ISAs.

Qualitative characteristics –. We appreciate the effort taken to develop, articulate and describe these criteria, nevertheless we suspect the degree of subjectivity may mean they are not implementable. There are many of these and their application will be highly subjective. LCE is a new concept and is highly subjective and hard to define. We think that quantitative criteria are needed to supplement or supersede qualitative.

As indicated in the ED, the IAASB debated the use of quantitative or other exemption thresholds or more specific criteria to scope the standard but *“agreed that it would not be practicable for the IAASB to define exemption thresholds or other criteria about what may constitute an audit of an LCE that would be capable of consistent global application because of, for example, the varying sizes of economies and sophistication of jurisdictions.”*

Nevertheless, we suspect there is a strong correlation between size and complexity. Small entities are usually less complex than large. Furthermore, the most SMEs share the qualitative characteristics. Size criteria are objective, recognizable, understandable, and, in many jurisdictions, is a tried and tested approach. In the EU size thresholds have been used successfully for many years in policy and regulation including in the field of accounting and auditing.

We therefore propose the IAASB to reconsider the size as quantitative criteria – and provide some guidance as to how thresholds can be determined at jurisdiction level e.g., relative to mean or median sizes of companies in that jurisdiction or else using thresholds already commonly used in that jurisdiction.

Furthermore, the IAASB might wish to explicitly state that all SMEs, defined according to size criteria decided at national level, are automatically considered as LCE unless there is strong evidence to the contrary, such as they exhibit a characteristic that indicates they are complex. Hence, we wonder whether there should be a rebuttable assumption that all companies that meet regionally or nationally determined size criteria are classified as less complex and as such eligible for using the standard.

We suspect that many national standard setters and regulators in Europe will, to the extent to which EU Directives allow, apply simple size criteria instead or as well as the qualitative criteria. Guidance to help them do so with a degree of consistency from one jurisdiction to another would be welcome

5. Regarding the Authority Supplemental Guide:

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

Response:

We believe the guide is very helpful in understanding the Authority.

The guide is in fact essential given the multiple facets to Authority as summarized in the diagram in paragraph 50. If the IAASB finally determines that size criteria be the main or overriding criteria for the determination as to the scope of the standard, we think will be necessary to provide some guidance as to how individual jurisdictions can go about the determination on appropriate size thresholds.

In Spain, the audit reports of SME entities were 87% of the total published, according to ICAC source. In this sense, the importance of this standard is huge.

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

Response:

We have no suggestions as to other matters that should be included in the guide except as mentioned in our response to 5 (a) guidance on establishing appropriate size thresholds.

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:

Regarding the perception of audit quality, we consider it is vital that audits conducted in accordance with the new standard will be widely perceived and recognized as producing an audit that is of the same high quality as that of an audit using the full ISAs. This will demand a universal, consistent, and robust information campaign from all authoritative sources.

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 are agreeable with the approach to how the ISA requirements have been incorporated in the proposed standard.

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

Response:

We agree with this approach

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

Response:

We agree with the inclusion of these principles.

- (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 agree with the approach to EEM including content, sufficiency, and its presentation. We, however, consider that the content of the EEM is sometimes quite complicated and lengthy. We recommend further efforts to reduce and simplify.

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 welcome the overall design and structure. We believe the design and structure to be logical and effective. Indeed, in following the flow of the audit, in contrast to the full ISAs that are organized topic by topic, the standard is more easily read and understood.

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:

We believe the content to be robust, proportionate, and complete. Notwithstanding this, our review has revealed the existence of some complicated and lengthy sentences that are 'lifted' almost verbatim from the ISAs. We recommend simplifying and shortening these sentences.

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 agree with the approach taken for auditor reporting requirements.

We welcome the fact that the section 'Basis for Opinion' makes it clear that the audit is performed in accordance with the ISA for LCE standard.

11. With regard to the Reporting Supplemental Guide:
- (a) Is the support material helpful, and if not, why not?

Response:

We find the Reporting Supplemental Guide helpful.

Indeed, guidance of this nature, outside the body of the standard is especially helpful and in time support material might extend to most if not all aspects of the standard in the way that the IFAC ISA Guide does for the ISAs.

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

Response:

We do not any other matters in relation to reporting, other than in relation to audit of group financial statements, 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:

We have no other proposals for improvement except as indicated above in relation to audit group financial statements.

We are confident that the robust process followed in developing the standard has resulted in a high-quality standard that is accurate and complete.

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:

We recognize the challenges of transitioning. Challenges for transitioning work in both directions, both *to* and *from* the new standard. Section 4F focuses on *from* the ISA for LCEs and Section 4.6. deals with Initial Audit Engagements of the standard.

In the initial years after the new standard takes effect there will be many entities and their auditors having to address first time use of the new standard, many the first-time use of any audit standard. Over time as the new standard gets well established and is widely used, the number of LCEs transitioning to the new standard will decline.

Similarly in subsequent later years we expect to see LCEs either become complex or otherwise not eligible to continue using the standard and so having to transition to the ISAs. Section 4F seems to adequately deal with this direction of transition.

Our concern is that a single new element of complexity may cause an entity to no longer be classified as LCE, causing the auditor to have to transition to the full site of ISAs. This will create a burden that may be difficult to explain to an audited entity. Our suggestion above to lend more weight to size criteria might avoid the need for transition in these circumstances

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

Response:

We believe no further guidance may be necessary.

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

Response:

We agree with the proposed approach to the future updates and maintenance of the Standard and related supplemental guidance, which strikes an appropriate balance between having a relatively stable platform and ensuring the standard reflects prevailing best practice.

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

Response:

We agree to use the same approach as is used for the ISAs that is, allowing early adoption.

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

Response:

We think will be useful the development of a part for the ISA-800 series to be included in the ED-ISA for LCE.

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:

We think that the standard should be adopted by the Spanish Audit Authority. From our Audit Corporation (REA Auditores – CGE) we will make an effort and propose to be adopted. Additionally, we strongly believe that this standard must be included in the EU audit regulation in order to equalize the audit standards across Europe.

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

Response:

We believe the proposed standard effectively 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:

We are not aware of any other aspects of the proposed standard that may create challenges for implementation, other than those challenges addressed above.

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:

We do not believe there are any other matters that the IAASB should consider in terms of the form and content of the proposed standard. However, as we mention above, we believe there to be a significant challenge in promoting, positioning, and presenting the standard to the corporate reporting world.

Section 4G - Approach to Consultation and Finalization

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

Response:

We believe there will be an urgent need for support and guidance.

As we previously note, the standard, quite rightly, does not include guidance as such. Guidance for the most part is left out of the standards and included in separate non-authoritative documents produced by IFAC, PAOs and others.

We recognize the considerable training and education effort needed for the effective implementation of the standard. We therefore encourage the Board to collaborate with IFAC in developing appropriate support and guidance.

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:

We have not seen translation issues peculiar to this project.

This project presents the same of similar translation issues and challenges as confronted on any IAASB project.

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:

We believe this will provide a sufficient period to support effective implementation of the ISA for LCE.

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:

We support the inclusion of group audits.

Groups are not necessarily more complex than individual entities. This is especially the case when the management and ownership are concentrated in the hands of very few people: such groups tend to be managed as a single entity. Furthermore, if groups are scoped out then many LCEs that are part of a group may be required to conduct audits in accordance with full ISAs. Hence, we suggest that groups be scoped into the standard.

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:

We consider that the standard will be adopted and used even if group audits were excluded. However, the exclusion of groups will likely significantly limit the extent to which the standard is used.

- (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:

We are not a firm or practice.

Due to the most of the auditor reports are related as SMEs (see Question 5), the most of groups are consequently also SMEs.

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

Response:

As mentioned above groups are not necessarily more complex than individual entities. This is especially the case when the management and ownership are concentrated in the hands of very few people: such groups tend to be managed as a single entity. For example, a group formed by three LCE is consequently a LCE group itself. Hence, we suggest that groups be scoped in.

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:

We hold no strong view but slightly prefer Option 1.

Option 1 seems to be a simpler, less complex option. We prefer the 'bright lines' from using a proxy to leaving it for auditors to exercise their professional judgement in applying qualitative criteria. As we mention at the outset above, we have concerns over the subjectivity of using qualitative criteria to determine what is an LCE. We have similar concerns here. We think for consistent application and ease of use it is better to use Option 1.

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:

We cannot identify any other ways than the alternatives described above, nor can we think of any other proxies better than those presented.

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 have no strong view but have a slight preference for presenting all requirements pertaining to group audits in a separate Part. Hence, we suggest that simplified provisions from the ISA 600 suite be included in a separate Part.