



For the attention of Mr. Willie Botha
Technical Director
International Auditing and Assurance Standards Board
529 Fifth Avenue, 6th Floor
New York, New York, 10017
USA

[Submitted via IAASB website]

22 September 2019

Dear Mr. Botha,

IAASB Discussion Paper: Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the ISAs

We¹ appreciate the opportunity to comment on the IAASB's Discussion Paper (DP) for Audits of Less Complex Entities (LCEs).

Audits of LCEs represent a majority of audits conducted globally and are important to the stakeholders of those entities as well as to the confidence in economies more broadly. As the ISAs have evolved to address both the changing business environment and calls for greater specificity to address regulatory inspection findings, there has been a growing concern among many stakeholder groups that the associated increase in complexity and specificity in the standards is making them more difficult to apply, and is driving work effort, documentation and communication requirements that are perceived as excessive in less complex circumstances. Some stakeholders are beginning to question the ongoing appropriateness and relevance of the ISAs for audits of LCEs.

We support the IAASB in taking action. Maintaining global consensus and support for a consistent set of auditing standards applied across jurisdictions is important. It would be unfortunate and unhelpful if, as a result of frustration with the growing complexity in the ISAs, global consensus were to fragment, resulting in a myriad of different auditing standards promulgated in different jurisdictions. At the same time, whatever course of action the IAASB chooses to pursue, it is important that neither the value ("brand") of an "audit", nor the view that standards facilitate a high quality audit, be diminished, or be seen to have been diminished in the eyes of stakeholders.

There is a need to address overarching challenges as a priority

The DP highlights the various challenges that have been identified in applying the ISAs to an audit of an LCE. We agree with these challenges. Many of the challenges are, however, not exclusive to audits of LCEs. There are actions the IAASB should prioritise to address broader issues such as a lack of clarity in language used, undue complexity and prescription in requirements - including a shift to focusing on process rather than on outcomes - and the length of standards. Addressing these overarching issues would directly help in alleviating some of the concerns that are identified as also being challenges for audits of LCEs.

¹ This response is being filed on behalf of the network of member firms of PricewaterhouseCoopers International Limited and references to "PwC", "we" and "our" refer to the PwC network of member firms.

PricewaterhouseCoopers International Limited
1 Embankment Place
London WC2N 6RH
T: + 44 (0)20 7583 5000, F: + 44 (0)20 7822 4652



Maintaining a single set of auditing standards applicable to all audits is important

In addressing these overarching issues, our preference is to do so under an overall objective of maintaining a single set of auditing standards applicable to all audits. Such standards should set clear principles of what is to be achieved, use clear and unambiguous language and avoid complex sentence structures.

Standards should avoid excessive prescription and only include application material when it is deemed necessary to the appropriate understanding of the requirement (i.e., removing extraneous “educational” and unnecessary contextual information, as well as avoiding circumstances when it is included because of a lack of clarity in the requirement itself).

We are not convinced that efforts to date, including in the proposed revision of ISA 315, sufficiently address the various challenges that have been identified.

We suggest that the Board further explore an alternative structure for the standards. There are potentially a number of options that could be considered. For example:

- More clearly setting out what requirements apply in all cases and what requirements may apply in certain circumstances, such as when specific conditions exist or in the case of listed entity audits (often referred to as the “building blocks” approach). Greater use of conditional requirements, based on the characteristics of an entity and circumstances that may exist, may help in this regard.
- Including within each standard a new appendix or separate section setting out specific guidance on how the requirements in that standard may typically be expected to apply in the context of an LCE audit. This guidance would be able to also indicate any requirements that may not be expected to apply. We believe this would be more effective than interspersing guidance on “scalability” throughout the application material, as that is fragmented and doesn’t provide an overall picture of how the standard can be applied in a scalable manner in less complex circumstances.
- Relocating all requirements that are applicable to listed entity audits into a new “special considerations” standard, adopting a similar principle to that of ISA 600, which could facilitate shortening the foundational ISAs (helping to address the length and perception challenge) and encouraging a stronger focus on the base principles of the audit and what is necessary to provide a sufficient basis for obtaining sufficient appropriate audit evidence in all circumstances (helping to address the complexity and scalability challenge).

We believe one, or a combination, of the options above, would facilitate maintaining a single set of robust, yet scalable, standards that support the performance of consistent audits across the globe. Exploring these options would assist the Board in focusing on better articulating what work is core to all audits and distinguishing detailed requirements that stakeholders, in particular regulators, believe are appropriate for public interest entity (PIE) audits, including listed entities. Clear differentiation in the required documentation, communication and reporting requirements for PIEs and LCEs could be made too.

We believe that seeking a solution that retains one set of standards applicable to all audits is preferable for several reasons, which we describe in detail in our response to question 4 in appendix 1

of this letter. Although a separate standard for audits of LCEs could be developed (and may even be seen as preferable in some jurisdictions), that approach may give rise to some new challenges and could possibly adversely affect audit quality, or the perception of it, more broadly. In particular, we see a risk in creating a perception that “audits” of smaller entities provide less assurance than audits of PIEs. It is difficult to argue that both are a basis for “reasonable assurance” if the expectations of the work to be performed and evidence obtained is fundamentally different (as opposed to the scalable application of the same set of standards).

If options to revise a single set of standards cannot be found on which all stakeholders can agree, the Board would need to explore the option of a separate standard for audits of LCEs, as we do not believe the status quo can be sustained. However, we encourage the IAASB to first explore using a revised structure for the content of an ISA, and to engage with stakeholders to get feedback, before committing to the less preferable approach of developing an entirely separate standard for audits of LCEs.

Adopting a phased approach to revision

It is clear that the resources and capacity needed to conduct one large project to effect the level of change being called for would be significant, as would the option of developing a separate standard for audits of LCEs. Difficult choices regarding relative priorities vis-a-vis the Board’s current and planned projects will be necessary, for which not all stakeholders may agree. For example, a concerted focus on audits of LCEs for an extended period may reduce time available for priorities that others see as more important, for example, in relation to audits of listed entities. There will be significant strategic decisions that would need to be made, taking into account the views and priorities of all stakeholders, and it is important that all key stakeholders accept the final proposed plan.

A rolling or phased revision of the ISAs, based on one or a combination of the options we describe above, may also present similar resource and capacity challenges and be seen as not sufficiently timely in responding to the concerns being expressed now. However, we believe this to be the most appropriate path for the Board to take and would allow other projects that are seen to be of priority to also progress concurrently. Based on the feedback to this DP, the IAASB may identify ISAs that are seen as most challenging and that, consequently, should be prioritised for revision.

Developing a prioritised rolling program in this manner may address those challenges that stakeholders are most concerned by such that it would be acceptable that other, lesser, concerns be addressed over time. Even under such an approach, the Board may wish to consider whether temporary guidance that could be developed and issued on an expedited basis would help, pending revision of all priority ISAs, in addressing the most significant areas of challenge identified by respondents.

Addressing specific challenges

In our view, the challenges identified relating to specific ISAs need to be bifurcated between aspects of the ISAs that are generally seen as challenging to apply (and which, potentially, may be viewed even more so in the context of an audit of an LCE), and aspects of requirements of the ISAs that respondents do not believe are relevant/necessary in the audit of an LCE. Similar to the overarching issues we refer to above, addressing those aspects of the ISAs that are generally seen as challenging would further address some of the concerns applicable to audits of LCEs.



Exploring alternatives to audit

The DP focuses solely on addressing challenges in applying the ISAs to audits of LCEs. We believe there may also be demand for some other form of assurance service that is not an audit (and is something more than a limited assurance review). The IAASB could seek views from national standard-setters, IFAC member firms and others about ideas and any initiatives in jurisdictions as to the potential form and characteristics of any such assurance service. As we note above, if a new assurance service was to be explored, it is important that this not be seen to undermine or diminish the value of an audit.

We provide further context to the above points in our responses to the detailed questions posed in the DP in Appendix 1 to this letter.

We would be happy to discuss our views further with you. If you have any questions regarding this letter, please contact Diana Hillier, at diana.hillier@pwc.com, or me, at james.chalmers@pwc.com.

Yours sincerely,

A handwritten signature in black ink that reads 'James Chalmers'.

James Chalmers
Global Assurance Leader

Appendix 1 - Responses to specific questions

1. We are looking for views about how LCEs could be described (see page 4). In your view, is the description appropriate for the types of entities that would be the focus of our work in relation to audits of LCEs, and are there any other characteristics that should be included?

Within the context of our overall view that a single set of standards should be maintained, as described in our cover letter, using the current definition of smaller entity as a starting point is sensible. The majority of entities that will be considered less complex will be smaller. However, we suggest the definition could be further enhanced in a number of respects.

With respect to part (a) of the definition, there are likely to be many entities that exhibit the characteristics set out in the definition of smaller entity but that are owned by larger, non-complex organisations. The reference to *“another enterprise that owns the entity provided the owner exhibits the relevant qualitative characteristics”* may therefore cause confusion as to whether this restricts the application of the definition to the stand-alone (statutory) audit of that entity. Separate considerations would also apply as to what standards may need to apply in the context of an “audit” of a less-complex component as part of a complex group audit.

Similarly, reference to having “one or more of the following” characteristics may need to be clarified to make clear that exhibiting one specific characteristic does not mean the entity can be considered an LCE if other characteristics indicate otherwise (e.g., an entity that has few lines of business and product lines, but whose transactions are complex, would be unlikely to be deemed to be an LCE). There may be merit in combining, in addition to clarifying, these two characteristics.

We also suggest that it would be more appropriate to replace the term “few” in several of the qualitative characteristics. By way of example, the fact that there are “few controls” is only appropriate if the nature of the entity means that there is not a need for many controls, as distinct from an inadequate system of internal control. Likewise, the breadth of the range of management and personnel responsibilities itself may not always be a reliable indicator of complexity. In smaller organisations, an individual may have a broad range of responsibilities, some of which may involve one or more complex matters.

Consideration of the entity’s industry and the basis of accounting used may also be relevant in the determination of whether an entity is an LCE.

In addressing the issue that there are larger entities that may have very simple, less complex business models or operations, and smaller entities that are complex, it will be important to expand upon the final sentence of the definition to illustrate this point more clearly. This could be through appropriate guidance materials or application material accompanying the definition, should it be incorporated into any future separate standard.

Specifically, to avoid ambiguity, we suggest the IAASB address the question of whether any form of listed entity can be considered an LCE. There are many entities that may be simple holding companies, or entities with very simple operations, but that have issued listed debt. Perhaps such entities could still be included in the definition of an LCE if they otherwise exhibit characteristics of an LCE.

There will inevitably be circumstances where the decision as to whether the definition applies to an

entity is a matter of judgement. Should the IAASB choose to move forward with a separate standard, which is not our preferred solution, it may be necessary to develop more directive guidance as to factors that need to be given greater weight, or that may indicate it may not be appropriate to determine an entity as being an LCE, to assist the auditor in documenting their professional judgement and rationale in making that determination. This would help to mitigate potential risks to audit quality that could arise if a separate standard was applied to an entity that should not be considered an LCE.

2. Section II describes challenges related to audits of LCEs, including those challenges that are within the scope of our work in relation to audits of LCEs. In relation to the challenges that we are looking to address:

- a. What are the particular aspects of the ISAs that are difficult to apply? It would be most helpful if your answer includes references to the specific ISAs and the particular requirements in these ISAs that are most problematic in an audit of an LCE.**

The matters identified by the IAASB in section II of the DP are a fair summary of the challenges most frequently raised with respect to applying the ISAs to audits of LCEs.

In addition to practical challenges in the application of aspects of some ISAs, there is a perception challenge that also needs to be addressed. The length and complexity of recent new and revised standards has been a clear factor in increasing the level of concern about the understandability and scalable application of the standards.

Challenges in applying the ISAs, such as the complexity and clarity of language used, understandability, and length of the standards are not necessarily unique to audits of LCEs. The ISAs, as a body, are also becoming more challenging to apply for non-LCE audits. These issues need to be addressed holistically as a priority.

We suggest bifurcating this question between: (i) aspects of the ISAs that are generally seen as challenging to apply (and which, potentially, may be viewed even more so in the context of an audit of an LCE); and (ii) aspects of requirements of the ISAs that respondents do not believe are always relevant/necessary in the audit of an LCE.

The latter needs to be addressed, but we would encourage the Board to focus initially on the first category of challenges. Taking appropriate action to address these broader challenges in applying the ISA requirements may also help to alleviate some of the concerns that are identified as challenges for audits of LCEs. We have provided further views on this matter in our response to question 4 in relation to the possible actions the IAASB may take.

Within that context, we include in Appendix 2 aspects of the ISAs that we suggest be given further consideration by the IAASB, because we believe they either: (i) lack clarity as to what is required, leading to questions as to how the requirement can be scaled; or (ii) can be seen as unduly onerous when applied to an audit of an LCE.

- b. In relation to 2a above, what, in your view, is the underlying cause(s) of these challenges and how have you managed or addressed these challenges? Are there any other broad challenges that have not been identified that should be considered as we progress our work on audits of LCEs?**

The increased level of prescription in requirements and shift to focus more on process rather than on outcomes has, in our view, been the main underlying cause. Over time, there has been a trend that has seen a perceived need for more definitions, more specific requirements and extensive additional guidance to seek to explain what is expected of the auditor, driving more of a compliance mindset and a focus on documenting compliance, rather than focusing on the objective of the auditor's procedures and the key concepts in auditing.

In order to overcome some of the challenges described in Appendix 2 our Network has developed practical materials to help engagement teams meet the requirements of the standards. For example:

- Guidance regarding the identification of internal controls within business processes, including a list of commonly applicable controls for various business processes;
- A standard testing plan to be executed when off-the-shelf IT systems are used by the entity; and
- A practice aid that includes common ("less-complex") accounting estimates to help identify appropriate financial reporting framework requirements, methods, assumptions and data used to develop those accounting estimates as well as common internal controls that management might put in place to address the business risks related to the accounting estimates.

Other challenges

Section I of the DP describes the evolving business environment and the effect that is having on the ISAs. Specifically, within this section the IAASB identifies that the increased robustness of regulatory and oversight body inspections has resulted in calls for more specificity in the requirements against which audits can be inspected.

This "environmental" factor is not directly addressed in the analysis of challenges in section II. There is a need to directly acknowledge that the expectations of regulatory and oversight bodies, who are primarily focused on audits of PIEs, including listed entities, and expectations of those stakeholders representing SMEs and SMPs are increasingly divergent.

A direct consequence of a drive to increased specificity in requirements is, as section II highlights, a shift towards a more prescriptive, compliance-driven, approach and longer standards, which has fuelled concerns about scalability.

In contemplating the possible actions set out in section III, specifically Actions A and C (i.e., actions other than developing a separate standard for audits of LCEs), this inherent tension is worthy of consideration. For example, is it possible to revise the ISAs and meet the expectations of all stakeholders? Some actions, such as increased use of conditional requirements, and potentially exploring an alternative structure for the standards, as suggested in our cover letter, may create a framework making this possible.

The IAASB is already aware of the need to revise several ISAs to better address the use of technology. While this too is not a challenge exclusive to audits of LCEs, and perhaps less of a challenge compared to audits of much larger entities, there are aspects of the ISAs that are viewed as increasingly dated/onerous/redundant in light of advancements in technology tools available for use in performing an audit. The cumulative effect of such perceptions, combined with the concerns around scalability and prescription in standards, adds to the weight of concern around the application of the

ISAs to audits of LCEs. Progressing the IAASB's work on ISA 500 and technology is one element in the overall approach to addressing those broader issues we describe in response to part (a).

3. With regard to the factors driving challenges that are not within our control, or have been scoped out of our exploratory information gathering activities (as set out in Section II), if the IAASB were to focus on encouraging others to act, where should this focus be, and why?

With respect to legal and other requirements for an audit, we agree with the IAASB's analysis that this is a jurisdictional matter. However, it would be useful for the IAASB to obtain an understanding from jurisdictions whether any such decisions around audit exemption thresholds are driven, in any respect, by the perceived challenges in applying the ISAs.

Related to the above, the DP focuses solely on addressing challenges in applying the ISAs to audits of LCEs. The IAASB scoped out of its exploratory activities consideration of whether engagements other than audits would more directly benefit the SME sector. Where an audit continues to be mandated, we believe it is important that the IAASB address the challenges described in the DP. However, we also believe there may be demand for some other form of assurance service that is not an audit (and is something more than a limited assurance review). This may be a more robust solution, for example, than the potential for a diluted set of audit procedures in a separate standard that still purports to be an audit that results in a "reasonable assurance" audit opinion. It is important that, whatever action the IAASB chooses to take, the value ("brand") of an audit must not be diminished. The IAASB could seek views from national standard-setters, IFAC member firms and others about ideas and any initiatives in jurisdictions as to the potential form and characteristics of any such engagement.

We believe IFAC has a key role to play in promoting the value of audit and in seeking to address the challenges identified with respect to public expectations and understanding of an audit. IFAC could take a lead in the debate over the future of audit, working with national standard-setters and others, allowing the IAASB to focus on analysing and responding to the feedback received. We believe it would, however, be important for the IAASB to be consulted on any such IFAC initiative.

4. To be able to develop an appropriate way forward, it is important that we understand our stakeholders' views about each of the possible actions. In relation to the potential possible actions that may be undertaken as set out in Section III:

a. For each of the possible actions (either individually or in combination):

- i. Would the possible action appropriately address the challenges that have been identified?**
- ii. What could the implications or consequences be if the possible action(s) is undertaken? This may include if, in your view, it would not be appropriate to pursue a particular possible action, and why.**

We support retaining a single set of auditing standards applicable to all audits that set clear principles of what is to be achieved, are scalable to audits of varying circumstances, use clear and unambiguous language and avoid complex sentence structures. This view is based on our analysis of the pros and cons of the actions described by the IAASB in the DP, which we comment on below.

We believe standards should avoid excessive prescription and only include application material that is



deemed necessary to the appropriate understanding of the requirement (i.e., removing extraneous “educational” and unnecessary contextual information, as well as avoiding circumstances when it is included because of a lack of clarity in the requirement itself).

We suggest that the Board further explore an alternative structure for the standards. There are potentially a number of options that could be considered. For example:

- More clearly setting out what requirements apply in all cases and what requirements may apply in certain circumstances, such as when specific circumstances apply or in the case of listed audits (often referred to as the “building blocks” approach). Greater use of conditional requirements, based on the characteristics of an entity and circumstances that may exist, may help in this regard.
- Including within each standard a new appendix or separate section setting out specific guidance on how the requirements in that standard may typically be expected to apply in the context of an LCE audit. This guidance would be able to also indicate any requirements that typically may not be expected to apply. We believe this would be more effective than interspersing guidance on “scalability” throughout the application material, as that is fragmented and doesn’t provide an overall picture of how the standard can be applied in a scalable manner in less complex circumstances.
- Relocating all requirements that are applicable to listed entity audits into a new “special considerations” standard, adopting a similar principle to that in ISA 600, which could facilitate shortening the foundational ISAs (helping to address the length and perception challenge) and encouraging a stronger focus on the base principles of the audit and what is necessary to provide a sufficient basis for obtaining sufficient appropriate audit evidence in all circumstances (helping to address the complexity and scalability challenge).

Action A

We believe one, or a combination, of the options above, would facilitate maintaining a single set of robust, yet scalable, standards that support the performance of consistent audits across the globe. Exploring these options would assist the Board in focusing on better articulating what work is core to all audits and distinguishing detailed requirements that stakeholders, in particular regulators, believe are appropriate for audits of PIEs, included listed entities. Clear differentiation in the required documentation, communication and reporting requirements for PIEs and LCEs could be made too.

As we discuss in our response to question 2, there are also actions we believe the IAASB should prioritise. Those actions, several of which are encompassed within Action A on revising the ISAs, should address the broad challenges relating to the complexity and clarity of language used, and the length of standards.

With respect to revising the broader suite of ISAs, while perhaps representing the “perfect world” scenario, it is clear that the resources and capacity needed to conduct one large project to effect the level of change being called for would be significant. Difficult choices regarding relative priorities vis-a-vis the Board’s current and planned projects will be necessary, for which not all stakeholders may agree. For example, a concerted focus on audits of LCEs for an extended period may reduce time available for priorities that others see as more important, for example, in relation to audits of listed entities. There will be significant strategic decisions that would need to be made, taking into account

the views and priorities of all stakeholders, and it is important that all key stakeholders accept the final proposed plan.

A rolling or phased revision of the ISAs, based on one or a combination of the options we describe above, may also face similar resource and capacity challenges as well as being seen as not sufficiently timely in responding to the concerns being expressed now. However, we believe this to be the most appropriate path for the Board to take and would allow other projects that are seen to be of priority to also progress concurrently. Based on the feedback to this DP, the IAASB may identify ISAs seen as most challenging that should be prioritised for revision.

Developing a prioritised rolling program in this manner may address those challenges that stakeholders are most concerned by such that it would be acceptable that other, lesser, concerns be addressed over time. Even under such an approach, the Board may wish to consider temporary guidance that could be developed and issued on an expedited basis that would, pending revision of all priority ISAs, help with addressing the most significant areas of challenge identified by respondents.

Action B

Although a separate standard for audits of LCEs could be developed, and may even be seen as preferable in some jurisdictions, that approach may give rise to some new challenges and could possibly adversely affect audit quality, or the perception of it, more broadly.

Further to our overarching comments in response to this question, it is not clear to us why many of the “possible features” of a separate standard should not be guiding factors for the development of standards generally, rather than solely for an audit of an LCE. We believe if these features were applied to a revision of the existing standards, as described above, many of the concerns about auditing LCEs could be addressed while retaining a single set of standards.

We do not discount that having separate standards may enable those standards to be better tailored to the characteristics of the entities for which they are designed and related expectations of respective stakeholders, while also eliminating the inherent tension we describe in our response to question 2(b). However, we are concerned that in trying to develop a separate standard that is based on the ISAs this will:

- Challenge the maxim that “an audit is an audit”; and
- Risk creating a perception that “audits” of smaller entities provide less assurance than audits of PIEs. It is difficult to argue that both are a basis for “reasonable assurance” if the expectations of the work to be performed and evidence obtained is fundamentally different (as opposed to the scalable application of the same set of standards).

Dual standards may create resourcing challenges, as mobility of staff and partners between sectors would require processes to ensure appropriate training and experience for those working in each sector and/or moving between the sectors. Behaviours embedded when working primarily in one sector may not translate easily when working in the other sector. This could also have the potential for creating further barriers to entry and concentration of the audit market if some firms made a choice to only participate in one sector.

If options to revise a single set of standards cannot be found on which all stakeholders can agree, the Board would need to explore the option of a separate standard for audits of LCEs, as we do not

believe the status quo can be sustained. However, we encourage the IAASB to first explore using a revised structure for the content of an ISA, and to engage with stakeholders to get feedback, before committing to the less preferable approach of developing an entirely separate standard for audits of LCEs.

Building stakeholder consensus for any proposed solution is important. Outcomes that lack support risk a multitude of different, potentially inconsistent, approaches globally, which is an undesirable outcome that may create potentially significant challenges for multinational (group) audits as well as driving a lack of comparability across jurisdictions. In seeking to maintain global consensus and avoid global fragmentation, it is therefore important that the IAASB is able to effectively communicate to national standard-setters and professional bodies that are leading the development of “national” solutions how its actions other than the development of a separate standard are responsive to the challenges identified and are expected to be effective. That is true not just for audits of LCEs but also with respect to addressing the broader challenges identified in applying the ISAs, as described above.

Lastly, we note that we would need more information about the proposal to develop a separate standard based on an entirely different framework before we would feel able to provide meaningful and helpful input. However, for all the reasons set out above, pursuing a separate standard is not our preferred solution. Developing a standard based on a framework other than ISAs may also cause confusion for financial statement users and exacerbate questions about what constitutes an “audit” and how to reconcile the work effort needed to have reasonable assurance under an ISA audit with the work effort prescribed under such a separate standard, whether that be reasonable or some new level of assurance.

Action C

Action C is not mutually exclusive to the other actions presented in the DP. Whether supporting a revised and restructured body of ISAs, or a separate standard for the audit of LCEs, there will be some role for additional guidance. On its own, guidance would not, in our view, be an adequate response to the broader challenges identified within the DP. As we describe in our overarching points in response to this question, there are broader drafting and structural issues that the IAASB needs to address across the body of the ISAs.

Implementation support materials for new ISAs should be a presumption. The need for such materials as well as the nature and extent will vary based on the ISA in question, but these support tools are likely to be useful.

We recognise that a comprehensive guide to applying the ISAs for LCEs, or an IAPN, presents an opportunity to remove content from the underlying ISAs, therefore creating shorter, more readable standards. The trade-off of such an approach is to require auditors of LCEs to consult more than one source for guidance when applying the standards. Questions are also likely to arise as to the authority of such material and whether it is sufficiently clear as to how it addresses the expectations for work effort set by the requirements to which it relates.

Based on our views above, we believe that a structured revision of the ISAs, adopting one or a combination of the options we describe, would be more effective. However, recognising the development timeline for such a project, even on a phased basis, the Board may wish to consider whether temporary guidance that could be developed and issued on an expedited basis would help, pending revision of all priority ISAs, in addressing the most significant areas of challenge identified by



respondents..

- b. Are there any other possible actions that have not been identified that should be considered as we progress our work on audits of LCEs?**

No further actions identified with respect to audits of LCEs.

- c. In your view, what possible actions should be pursued by us as a priority, and why? This may include one or more of the possible actions, or aspects of those actions, set out in Section III, or noted in response to 4b above.**

See our overarching responses to part (a).

- 5. Are there any other matters that should be considered by us as we deliberate on the way forward in relation to audits of LCEs?**

The IAASB should consider how the IFAC SMP Committee could be more effectively engaged in its standard-setting projects and whether more direct outreach with other SMP stakeholders could address perceptions that there is insufficient input or representation of this sector in the board's work. See also our response to question 3 on exploring alternative forms of engagement.

Given the nature and complexity of the revisions to ISA 540 and ISA 315, the IAASB should closely monitor the implementation of these standards and stand ready to address potential concerns in a timely manner. A formal post-implementation review of these standards, in particular focusing on how the standards are being applied in audits of LCEs, would also be useful to determine whether the revisions have achieved the IAASB's intended objectives



Appendix 2 - Aspects of ISAs that are difficult to apply in audits of LCEs

Listed below are key areas we have identified where common challenges occur in applying ISA requirements and guidance on LCE audits. Our Network has developed additional guidance in these areas to assist our engagement teams with effective application. Where applicable, potential ISA guidance clarifications that might be helpful are noted for consideration:

- ISA 240 paragraph 33(a) - It can be challenging to determine an appropriate extent of journal entries testing in LCE audits when there are limited fraud risk criteria identified and non-complex systems are used. Additional guidance and/or illustrative examples would be helpful when non-complex systems are used by the entity and all journal entries are treated as manual.
- ISA 315 paragraphs 11-24 - There are challenges in determining the appropriate extent of understanding of the system of internal control, in particular evaluating design and implementation of relevant control activities and General IT controls, especially when the entity's system of internal control and information system is non-complex (e.g., an off-the-shelf system) and when there is limited formal documentation supporting relevant controls.
- ISA 320 paragraph 10 (and paragraph 4) - There appears to be diversity in practice when determining materiality benchmarks and rules of thumb in LCE audits. Additional guidance and/or illustrative examples would be helpful to acknowledge how users of the financial statements may differ, and how this may affect judgments about materiality in those audits. For example, additional application guidance to address circumstances where there are a very limited number of users of the financial information (e.g., local authorities and management) would address a very common circumstance.
- ISA 330 paragraph 10(b) - It can be difficult to determine the appropriate nature and extent of testing of "indirect" General IT controls, especially when the entity uses non-complex 'off-the-shelf' systems that they cannot modify. More guidance and examples may be helpful to clarify the nature and extent of tests of controls for entities that use packaged software applications (off-the-shelf systems).
- ISA 540 (Revised) - In planning for our Network implementation of ISA 540 (Revised), when considering simpler, lower risk estimates, the work effort related to the risk assessment and documentation requirements seem disproportionate and outweigh the perceived benefits to audit quality for LCE audits. Further guidance and/or illustrative examples on how ISA 540 can be applied in a more scalable manner would be helpful.