



# PROPOSED REVISIONS TO THE DEFINITIONS OF LISTED ENTITY AND PUBLIC INTEREST ENTITY

Issued 30 April 2021

ICAEW welcomes the opportunity to comment on the exposure draft on Proposed Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code published by the International Ethics Standards Board for Accountants on 29 January 2021 a copy of which is available from this [link](#).

This ICAEW response of 30 April 2021 reflects consultation with ICAEW technical committees including the Ethics Standards Committee which includes representatives from public practice and the business community. The Committee is responsible for ICAEW policy on ethics issues and related submissions to legislators, regulators and other external bodies.

We support the overarching objective of increasing confidence in the audit of entities of public interest, and agree the independence of auditors is key to achieving this. In addition to independence, it is important that there is a focus on improving audit quality.

We also support the proposed approach of having broad categories of entity within the PIE definition that local standard setters can then refine for their market. We are concerned however that some jurisdictions could scope out some categories entirely without reasonable justification and that there should be a de minimis level of implementation for a jurisdiction to be in compliance with the standard.

We have received mixed views on whether firms should have a responsibility to determine if an entity should be treated as a PIE for audit purposes. If this requirement were brought in it is important that safeguards are put in place to reduce the risk of firms being exposed to criticism by local regulators.

Transparency of whether an entity has been treated as a PIE for audit purposes will be important to increase trust for users of accounts. We therefore support disclosure within the audit report that an entity has been treated as a PIE, and a brief explanation of what the implications are in terms of restricted non-audit services and other independence provisions.

Consistency between standard setters is important so we would encourage there to be alignment between the IESBA and IAASB in terms of differential requirements applying to PIEs.

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## KEY POINTS

### Objective of proposed changes

1. We support the overarching objective of increasing confidence in the audit of entities of public interest, and agree the independence of auditors is key to achieving this. In addition to independence, it is important that there is a focus on improving audit quality.
2. We also support the proposed approach of having broad categories of entity within the PIE definition that local standard setters can then refine for their market. We are concerned however that some jurisdictions could scope out some categories entirely without reasonable justification and that there should be a de minimis level of implementation for a jurisdiction to be in compliance with the standard.
3. We have received mixed views on whether firms should have a responsibility to determine if an entity should be treated as a PIE for audit purposes. If this requirement were brought in it is important that safeguards are put in place to reduce the risk of firms being exposed to criticism by local regulators.
4. Transparency of whether an entity has been treated as a PIE for audit purposes will be important to increase trust for users of accounts. We therefore support disclosure within the audit report that an entity has been treated as a PIE, and a brief explanation of what the implications are in terms of restricted non-audit services and other independence provisions.
5. Consistency between standard setters is important so we would encourage there to be alignment between the IESBA and IAASB in terms of differential requirements applying to PIEs.

## ANSWERS TO SPECIFIC QUESTIONS

### ***Question 1. Do you support the overarching objective set out in proposed paragraphs 400.8 and 400.9 as the objective for defining entities as PIEs for which the audits are subject to additional requirements under the Code?***

6. We support the objective of increasing confidence in the audit of financial statements for entities of public interest. Independence of auditors is a key element of ensuring trust by stakeholders in the work an auditor undertakes.
7. In our view, some of the proposals address perceived threats only, rather than actual threats to independence of auditors. While perceptions are important, any such measures should go hand in hand with measures to improve audit quality. The findings of recent high-profile audit failures indicate that the problem is principally one of application of auditing and quality control requirements rather than an underlying problem with current independence provisions.
8. We also support the concept of significant public interest in the financial condition of an entity, rather than a broader interest in the entity's activities, which would be too wide a scope for an assessment of PIE status when considering auditor independence. Given the increasing expectation for auditors to review non-financial information relating to an entity, perhaps 'financial condition' will need to include all aspects of the financial statements.
9. We note however that there may be an expectation gap in the eyes of the public about the scope of public interest that these provisions seek to address, so additional clarity both in the Code and the audit report may be necessary to clarify what is intended by those entities within the revised definition of a PIE.

**Question 2. Do you agree with the proposed list of factors set out in paragraph 400.8 for determining the level of public interest in an entity? Accepting that this is a non-exhaustive list, are there key factors which you believe should be added?**

10. The factors listed in 400.8 are an appropriate list to consider when determining the level of public interest in an entity. We would note however that the final factor – the potential systemic impact on other sectors and the economy as a whole in the event of financial failure of the entity – is subjective and difficult to evaluate. We would also question whether the list of factors in 400.8 would more logically sit later in section 400, specifically following the new requirement in R400.16. This would mean that all the factors to consider would be situated together, rather than users of the code needing to refer to both 400.8 and the additional list in 400.16 A1, which could prove confusing, subject to our comments below.
11. Greater clarity would also be welcome on whether the factors listed in 400.8 and 400.16 A1 have more than one purpose: - specifically whether the factors in 400.8 are solely criteria for a local standard setter to consider in refining its jurisdictional definition of a PIE; and those in 400.16 A1 are solely for firms to use in considering whether they should treat an entity as a PIE; or instead whether both local standard setters and firms should consider both lists of factors for their differing purposes.
12. We note that the text in R400.14 is drafted as ‘a firm shall treat an entity as a public interest entity....’ rather than text requiring the local standard setter to use the list in that section as the starting point for determining the appropriate PIE definition in their jurisdiction. Perhaps the proposed sections 400.8 onwards should be split into those sections with requirements for local standard setters, and those sections containing requirements for firms, and clearly setting out which material applies to who.

### Approach to Revising the PIE Definition

**Question 3. Do you support the broad approach adopted by the IESBA in developing its proposals for the PIE definition, including:**

- **Replacing the extant PIE definition with a list of high-level categories of PIEs?**
  - **Refinement of the IESBA definition by the relevant local bodies as part of the adoption and implementation process?**
13. Given the significant international variations in legislation, regulation and market characteristics, we agree that a broad approach to a global PIE definition should be one of high-level categories with subsequent refinement. The power of local bodies to refine the IESBA definition is crucial to reflect territory-specific legal regimes and market context.
  14. There needs to be a de minimis standard of adoption of the IESBA PIE definition for a jurisdiction to be able to claim that it has implemented the requirements of the Code in relation to PIEs. As the proposed provisions are drafted, a jurisdiction could choose to completely exempt one or more of the proposed categories of PIE from their local definition without needing to justify its exclusion. This would undermine the objective of enhancing the trust in the financial statements of PIE entities and could result in a lower minimum standard than currently exists. In any event it is important that there is transparency on whether an entity has been treated as a PIE for users of accounts.
  15. We also note that for large international firms the change in approach to definition of a PIE is likely to lead to additional complexity. At present there is some certainty from having a global minimum standard of PIE definition, given that most jurisdictions do not add to the IESBA requirement. The proposed changes would remove this comfort and would make it necessary to have knowledge of the PIE definition in each country, if as expected each jurisdiction’s regulator exercises their right to refine the definition.

## PIE Definition

**Question 4. Do you support the proposals for the new term ‘publicly traded entity’ as set out in subparagraph R400.14(a) and the Glossary, replacing the term ‘listed entity’? Please provide explanatory comments on the definition and its description in this ED.**

16. A broader definition is welcome to avoid a lack of clarity around definitions of a regulated exchange, and the classification of securities and debt in different jurisdictions.
17. We note that the term ‘publicly traded entity’ is defined in the glossary to the Code as ‘An entity that issues financial instruments that are transferrable and publicly traded.’ We suggest an alternative description as the definition of publicly traded entity as follows:

*‘An entity having issued transferrable financial instruments which are traded on a stock exchange or other facilitated mechanism.’*

This makes no distinction between retail and institutional investors and would include all market and Over The Counter trading.

**Question 5. Do you agree with the proposals for the remaining PIE categories set out in subparagraphs R400.14 (b) to (f)?**

18. The UK’s Financial Reporting Council Ethical Standard (‘FRC ES’) defines a PIE as follows (subject to certain criteria):

- (a) An issuer whose transferable securities are admitted to trading on a UK regulated market;*
- (b) A credit institution*
- (c) An insurance undertaking*

*No other entities have been specifically designated in law in the UK as public interest entities.*

For comparison purposes, we note that the proposed IESBA definition of a PIE is as follows:

*R400.14 For the purposes of this Part, a firm shall treat an entity as a public interest entity when it falls within any of the following categories:*

- (a) A publicly traded entity;*
- (b) An entity one of whose main functions is to take deposits from the public;*
- (c) An entity one of whose main functions is to provide insurance to the public;*
- (d) An entity whose function is to provide post-employment benefits;*
- (e) An entity whose function is to act as a collective investment vehicle and which issues redeemable financial instruments to the public; or*
- (f) An entity specified as such by law or regulation to meet the objective set out in paragraph 400.9.*

19. We note that there is some consistency between (a) to (c) of the list of high-level categories proposed by IESBA and the definition of a PIE in the FRC ES, albeit that the categories proposed by IESBA are wider than those in the UK definition. Entities with publicly traded (securities), credit institutions and insurance providers are entities in whose financial condition we would agree there is a significant public interest, and these form part of the UK’s PIE definition. In addition, the UK has independence provisions for Other Entities of Public Interest, which includes large private sector pension schemes. The broad categories of PIE proposed by IESBA would therefore have less of an impact in the UK than in other jurisdictions where the PIE definition is less developed, subject of course to the extent of refinement by the UK FRC.

20. We would welcome further clarity on which entities are considered as providing post-employment benefits as it is currently unclear as to whether this is intended to only apply to pension funds or whether it is also intended to apply to administrators of funds or employers that provide such benefits. Should this only apply to pension funds, the application of factors such as size or nature in determining whether a pension fund may be of public interest is easily understandable and can be refined by local bodies. Indeed, the Financial Reporting Council recently applied a size threshold as part of the definition of Other Entities of Public Interest, albeit that the additional independence restrictions only apply to the provision of non-audit services rather than the wider PIE provisions. In jurisdictions where the scheme accounts only show the scheme's assets (and not the scheme's liabilities) and are therefore effectively stewardship accounts, rather than indicating the financial condition of the scheme, the local regulator may determine that there is no public interest in the scheme accounts. To the extent that the inclusion of pension schemes within the PIE regime requires mandatory rotation of engagement partners/EQCRs or rotation between firms, caution may be needed due to the specialist nature of those equipped to fulfil these roles. There is a risk that non-specialist engagement partners/EQCRs would need to deliver the work which could have a negative impact on audit quality. In jurisdictions where pension schemes are already highly regulated, this possible negative impact on pension scheme audit quality may provide reasonable justification for schemes to be completely excluded
21. We note that categories (b), (c) and (e) make reference to 'the public'. The standard should clarify who the public constitutes – we would expect this to include both individuals and companies/businesses. Clarity would also be welcome on whether this term includes institutional investors.
22. We also note that charities have not been included as a category of PIE. We acknowledge that the broad nature of charities means their inclusion could be problematic. There may however be some merit in encouraging local regulators to consider whether certain types of charity should be included within their local definition under category (f).

***Question 6. Please provide your views on whether, bearing in mind the overarching objective, entities raising funds through less conventional forms of capital raising such as an initial coin offering (ICO) should be captured as a further PIE category in the IESBA Code. Please provide your views on how these could be defined for the purposes of the Code recognizing that local bodies would be expected to further refine the definition as appropriate.***

23. It is important that entities raising funds through new forms of capital are not excluded from being treated as PIEs, if the nature of the entity is such that there would be a significant public interest in its financial condition. It is also important that there is future proofing of the independence standards.
24. However, the interaction between financial regulatory oversight and audit independence provisions needs to be considered, as arguably the protection of investors is an issue for financial services regulators rather than ethical independence provisions. This may mean that entities raising funds through alternative forms of capital should not be included as a category of PIE at present.
25. If entities raising funds through new forms of capital were not included as a PIE category in the Code, local standard setters would still have the option to expand their country specific definition to include other forms of capital if they concluded that additional independence requirements were needed in their market. It would be helpful for the IESBA to include additional factors for domestic standard setters to take into account when considering the case for treating entities that raises funds through alternative forms of capital as PIEs.

## Role of Local Bodies

### **Question 7. Do you support proposed paragraph 400.15 A1 which explains the high-level nature of the list of PIE categories and the role of the relevant local bodies?**

26. We support the substance of 400.15 A1 in that it explains to local bodies that they have the freedom to refine the categories of PIE. Perhaps the paragraph could be rephrased in the interests of clarity to say that the bodies have the discretion to refine the PIE categories to take into account local law and regulation, and are able to determine the appropriate size thresholds for entities in their market.
27. As mentioned in paragraph 14 above, we do have some concerns that local standard setters would have the ability to scope out entirely certain categories of PIE without reasonable justification. To counter this risk, the standard should set out de minimis levels of adoption. However, should the IESBA believe this to be unworkable, the IESBA, through liaison with IFAC and its programme assessing SMO compliance, would need to monitor local standard setters, to see whether jurisdictions are making excessive use of the derogations.

### **Question 8. Please provide any feedback to the IESBA's proposed outreach and education support to relevant local bodies. In particular, what content and perspectives do you believe would be helpful from outreach and education perspectives?**

28. The key feature of any outreach and education support should be clarity of the objective of the PIE definition and what the appropriate changes might be in a particular jurisdiction given local contextual factors. Application discussions should reference back to the contextual principles of the PIE definition.
29. As noted above, there would also be an important role for the IESBA (via IFAC) in keeping sight of whether jurisdictions have sought to scope out any categories of PIE entirely without reasonable justification.

## Role of Firms

### **Question 9. Do you support the proposal to introduce a requirement for firms to determine if any additional entities should be treated as PIEs?**

30. As the IESBA has identified, there are a number of factors that could influence whether there would be a significant public interest in the financial condition of an entity. In reality, not all of these factors can be adequately assessed by a local regulator in every instance to fully capture all appropriate entities. However we have received mixed views on whether there should be an obligation on firms to consider whether entities should be treated as PIEs for audit independence purposes. If this requirement was introduced, we believe some additional safeguards would be necessary as set out in the paragraphs below.
31. There is a risk that local regulators will scrutinise the conclusions reached by firms in determining whether an entity should be treated as a PIE particularly where more than one firm has acted as auditor to an entity over a period of time, and the firms have reached different conclusions on the entity's PIE status. While the factors listed in paragraph 400.16 A1 seem logical issues to consider in performing an assessment of whether there would be a significant public interest in the financial condition of the entity, there should be an encouragement for local regulators to issue detailed guidance to firms based on the factors that is tailored to their jurisdiction. This should reduce the risk of inconsistent classification of entities as PIEs.

32. If this requirement were introduced, we would recommend that the possible challenges for firms in determining whether an entity should be treated as a PIE be kept under review in the post implementation period.

**Question 10. Please provide any comments to the proposed list of factors for consideration by firms in paragraph 400.16 A1.**

33. Please see our comments in response to question 9 above. Some further clarity may also be needed in 400.16 A1 to specify (if this is the paragraph's intention) that:
- the list of factors is non-exhaustive
  - the requirement for firms to consider PIE status of an entity is in addition to the position taken by local law and regulation, and that the firm may disagree with the conclusion reached by local law/regulation – but only to add additional entities as PIEs, not to remove them.

### Transparency Requirement for Firms

**Question 11. Do you support the proposal for firms to disclose if they treated an audit client as a PIE?**

34. Yes, given the objective of increasing confidence in the audit work that has been performed on the financial statements, it is important that stakeholders are aware whether an entity has been treated as a PIE or not. There should be a disclosure of whether the entity has been treated as a PIE, regardless of whether that is under local standards or because the firm has concluded that the entity should be treated as such.

**Question 12. Please share any views on possible mechanisms (including whether the auditor's report is an appropriate mechanism) to achieve such disclosure, including the advantages and disadvantages of each. Also see question 15(c) below.**

35. The auditor's report would seem to be a logical place to disclose the auditor independence provisions that have been applied and what the implications are in terms of restricted non-audit services and other independence provisions. To avoid an unnecessarily long auditors report, detail of the provisions could be included in the disclosure of non-audit services provided by the auditor.

### Other Matters

**Question 13. For the purposes of this project, do you support the IESBA's conclusions not to:**

- (a) **Review extant paragraph R400.20 with respect to extending the definition of 'audit client' for listed entities to all PIEs and to review the issue through a separate future workstream?**
- (b) **Propose any amendments to Part 4B of the Code?**

36. Given the wide-reaching changes proposed to the definition of a PIE, we would support the IESBA's conclusion to review the definition of audit client as a separate workstream.
37. In addition, on the basis that the objective of the proposed changes is to increase confidence in statutory audit, it would seem outside of the scope of the current project to propose amendments to Part 4B.

**Question 14. Do you support the proposed effective date of December 15, 2024?**

38. We would support the proposed implementation date of 2024 to allow time for jurisdictions to introduce the changes in their local regulations. Given the identified need to increase trust in audit and the public expectation that action is urgently taken on this issue, the IESBA should strongly encourage early adoption in jurisdictions that are able to do so.

#### Matters for IAASB consideration

**Question 15. To assist the IAASB in its deliberations, please provide your views on the following:**

- (a) ***Do you support the overarching objective set out in proposed paragraphs 400.8 and 400.9 for use by both the IESBA and IAASB in establishing differential requirements for certain entities (i.e., to introduce requirements that apply only to audits of financial statements of these entities)? Please also provide your views on how this might be approached in relation to the ISAs and ISQMs.***
- (b) ***The proposed case-by-case approach for determining whether differential requirements already established within the IAASB Standards should be applied only to listed entities or might be more broadly applied to other categories of PIEs.***
- (c) ***Considering IESBA's proposals relating to transparency as addressed by questions 11 and 12 above, and the further work to be undertaken as part of the IAASB's Auditor Reporting PIR, do you believe it would be appropriate to disclose within the auditor's report that the firm has treated an entity as a PIE? If so, how might this be approached in the auditor's report?***
39. We support the intention for both the IESBA and IAASB to establish additional requirements for the audits of Public Interest Entities. We would strongly encourage the IESBA and IAASB to take a consistent approach to the definition of a PIE to provide clarity for auditors and users of accounts.
40. On this basis the differential requirements within the IAASB standards should be extended to other categories of PIE to achieve consistent application of technical and ethical standards.
41. To increase trust in the audits of financial statements of PIEs it is important that there is transparency for the users of those accounts on whether the entity has been treated as a PIE for the purposes of auditing standards and ethical standards. The auditors report would seem the appropriate place to make that disclosure. See comments above.