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Consultation Paper: Collective Investment Vehicles and Pension Funds – Auditor Independence

Dear Mr Siong,

We value the opportunity to provide comments on the Consultation Paper issued by the International Ethics Standards Board for Accountants (IESBA or the Board) concerning collective investment vehicles (CIVs) and pension funds. This letter represents KPMG's views, incorporating feedback and insights from our global network.

We appreciate the IESBA seeking consultation to continue its course to “proceed cautiously before determining whether there is a need to revise the Code” as stated in the Board's Strategy and Work Plan, 2024-2027. The Consultation Paper explores the potential for gaps in the Code regarding the definition and treatment of related entities within the context of CIVs and pension funds. However, it is not clear from the paper that the IESBA has presented a problem that would necessitate amending the Code. Notably, as stated in the Consultation Paper, no cases of financial failure in this space in which “an auditor's lack of independence was a contributing factor” have been identified. This absence of examples, or a clear, well-supported means to notably increase auditor independence while balancing cost and disruption, indicates there is no urgent or compelling reason for the IESBA to undertake such a project.

The cost benefit and potential for unintended consequences must be considered against the perceived benefit of consistency in approach, which may not be achievable given the significant differences in investment schemes across jurisdictions and corresponding regulatory requirements. A fact-based impact analysis is crucial to support the need for the project and to understand the economic impact on investors and pensioners. This includes considering the cost of implementation and the likely restriction of auditor choice that funds and other impacted companies will face, which could potentially impact audit quality.

The considerations in the Consultation Paper query important points, but we believe the Code has been aptly written with the conceptual framework to capture any number of scenarios that are not explicitly addressed in a global code. And while the Code may not explicitly step into the space of CIVs and pension funds, jurisdictional regulators and

standard setters do address these schemes when they see a need for prescriptive requirements to drive independence. We also found the Consultation Paper's combination of CIVs and pension funds to be problematic, as they are fundamentally different in purpose, structure, and regulatory oversight. CIVs and pension funds serve distinct objectives, possess unique characteristics, and are often governed by separate regulatory frameworks with differing auditor obligations. The Consultation Paper does not sufficiently acknowledge or address these distinctions.

We highly value the principles-based, globally applicable nature of the Code and want to stress the importance of keeping this approach. A principles-based global code allows professionals to use their judgment effectively, especially in complex and varied situations. Conversely, an overly prescriptive approach hinders agility and the ability for thoughtful, principled decision making.

In the absence of a clearly demonstrated need, we believe it is prudent to maintain continuity in the Code to allow stakeholders a period of time to implement and adjust to recent significant changes. A constant stream of updates for very granular topics takes focus away from the main principles of the Code. A stable period would also give the Board time to objectively review how well recent changes to the Code are working and identify and respond to unintended consequences, ensuring that the Code develops in a balanced way, remaining centered on its overarching principles.

Regarding the matters raised in the Consultation Paper, we do not support the initiation of any further project in this area for the reasons stated above. CIVs and pension funds operate in highly regulated and diverse environments. It is important not to overstep or overcomplicate existing jurisdictional requirements.

Please contact Karen Bjune at kbjune@kpmg.com if you have questions on any of the points raised in this letter. We would be happy to discuss our views with you further.

Yours sincerely



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Appendix: Responses to the Consultation Questions

Question 1: Does the Code’s definition of “related entity” capture all relevant parties that need to be included in the auditor’s independence assessment when auditing CIVs/pension funds?

We believe the current definition of “related entity” remains appropriate as it specifically captures the entities to which the prescriptive independence requirements and prohibitions in the Code apply. Expanding the related entity definition and requirements without a clearly established need would lead to overly complicated situations, making the Code harder to apply consistently, limiting service provider choice and raising costs that would be passed on to investors and pensioners. Similarly, creating a new term within the Code to capture “connected” parties for a narrow use case does not seem to be naturally aligned to the overarching purpose of a global code. Introduction of this new term will also increase complexity of the Code as it is translated and incorporated into local professional standards globally.

CIVs, pension funds and other investment schemes differ substantially by jurisdiction and the related jurisdictional regulators and standard setters are best placed to understand and address independence concerns with such schemes in their jurisdictions. For the IESBA to embark on a global initiative without a clearly defined problem or benefit or a resulting impact analysis can lead to unnecessary complexity and unintended consequences.

Question 2: Do you believe the criteria set out are appropriate and sufficient to capture Connected Parties that should be considered in relation to the assessment of auditor independence with respect to the audit of a CIV/pension fund?

While we understand the intention of the term “Connected Parties,” the criteria lack the specificity needed for consistent application. Alternatively, case studies within non-authoritative material that use the criteria as guidance, such as factors to consider when identifying other parties that may need to be included when applying the conceptual framework, would support professionals in applying the Code effectively, especially in complex and varied situations.

The definition would not be suited to include in the Code due to the following:

- As we note above under Q1, creating a new term within the Code to capture parties for a narrow use case does not seem to be aligned to the overarching purpose of a global code.
- The term’s proposed definition would require additional clarification for the criteria if specific independence requirements were to be prescribed to such entities. Specifically:
 - Responsible for decision-making and operation: The term “responsible” may be open to varying interpretations on the degree of responsibility that would trigger this criterion. An entity could be responsible for decision making and operations to different degrees, and differences in this interpretation would lead to inconsistency in determining which parties should be considered for threats to independence.

- Able to substantially affect the financial performance: This criterion would be subjective without clearer conditions or thresholds to minimize discrepancies in interpretation. Without clarity, the criterion could be interpreted as applying to a party who selects investments (generating the return on investments), selects third-party service providers (incurring costs), funds the pension scheme with required or voluntary contributions, values the investments, or prepares accounting records and financial statements.
- In a position to exert significant influence over the preparation of its accounting records or financial statements: Contextualization would be required within the unique environments of CIVs and pension funds and the parties they contract for services. Identifying and monitoring such influence will be difficult due to the inherent complexity of these entities. For instance, when accounting functions are outsourced, the third-party provider may inadvertently fall within the scope of this criterion even if the audit client maintains ultimate responsibility for financial reporting. This could lead to an overly broad application of independence requirements, capturing relationships that do not pose genuine threats to auditor objectivity.
- Given the complexity of these investment schemes and their widespread use of service providers, there are cases where an entity will meet one of the criteria, yet relationships or interests of the auditor with that entity would not reasonably impair the firm's independence from the CIV or pension fund audit client. Case studies using the criteria as factors, including considering multiple factors, can show the importance of using professional judgment in an agile manner to apply the conceptual framework where threats to independence may truly exist.

***Question 3:** Where there are such Connected Parties, do you believe the application of the conceptual framework in Section 120 of the Code is sufficiently clear as to how to identify, evaluate, and address threats to independence resulting from interests, relationships, or circumstances between the auditor of the CIV/pension fund and the Connected Parties?*

The conceptual framework in Section 120 guides the professional accountant to consider objectivity without limiting its scope to specific entities. Through our internal socialization of the consultation paper, feedback did not indicate concerns in practice sufficient to support a project narrowly focused on this subject. Instead, internal discussions indicated that engagement teams regularly utilize the conceptual framework while also adhering to regulatory requirements when considering services to an entity that controls a CIV or pension fund through its decision-making ability.

While case studies on application of the conceptual framework to consider threats to independence from the key parties having control and significant influence over a CIV or pension fund could be created, this should be weighed carefully. Given the current shift to ease regulatory requirements, but more importantly without an impact analysis, we would urge the IESBA to focus their resources on post-implementation reviews of recently issued standards.

Question 4: *Is the conceptual framework consistently applied in practice for Connected Parties in CIV/pension fund audits?*

The application of the conceptual framework to Connected Parties can be challenging due to both the complexity and varied nature of CIVs and pension funds. As the IESBA acknowledged in its Strategy and Work Plan, 2024-2027, “these types of arrangements are much more diverse in structure, governance and size than deposit-taking institutions and insurers.”

Jurisdictional regulations may mandate specific considerations for independence, influencing how auditors apply the conceptual framework. For example, mandatory firm rotation serves as a guardrail in many jurisdictions. Additionally, regulations such as those requiring the separation of fund administration roles or independence from the operational management of the fund, work together with the conceptual framework to meet the reasonable expectations of the public interest in auditor independence. Adding a layer of complex requirements would disrupt market practices and, especially where jurisdictional regulations are already in place, severely limit auditor choice with the potential to negatively impact audit quality.

Expecting global consistency may not be feasible or necessary, given existing jurisdictional regulations. Where regulations are already in place, additional prescriptive requirements would have to be layered with the jurisdictional rules that have already been deemed sufficient by the regulator. We consider the local regulators to be best placed to prescribe any specific rules for the schemes in their jurisdiction, as well as to consider when they should be classified as public interest entities.

Question 5: *Are there certain interests, relationships, or circumstances between the auditor of a CIV/pension fund and its Connected Parties that should be addressed?*

The interests, relationships, or circumstances between auditors and Connected Parties that arise in the audit of CIVs and pension funds are nuanced due to the variety of Connected Parties, as well as the overarching complexity of the investment schemes themselves. Auditors should evaluate interests, relationships, and services where the CIV/pension fund is ultimately impacted by the interest, relationship or service, as these types of circumstances could pose potential threats to auditor independence. Relationships with the engaging party of the CIV or pension fund audit may also create threats to independence in appearance. Applying the conceptual framework in Section 120 allows consideration of significance and materiality to assess whether the relationships or services require safeguards to reduce threats to an acceptable level.

The development of non-authoritative material (NAM) is an option and, if crafted properly, could play a role in promoting consistent application of the conceptual framework, particularly in jurisdictions without specific regulations. NAM might cover scenarios such as assessing the independence threat from services provided to fund managers or the implications of relationships with advisors. This material could assist auditors in navigating the qualitative and quantitative aspects of these relationships, including when control and significant influence may exist outside of ownership relationships, thus providing a clearer

basis for evaluating and addressing any identified threats to independence. It would also remain interoperable with jurisdiction-specific approaches.

However, developing such material would require significant time and resources to ensure it was carefully researched and avoided misrepresentation or added complexity. Given the absence of a clearly identified problem and a low expected return on investment, we do not support allocating resources toward NAM at this time. Instead, we urge the IESBA to prioritize the allocation of staff resources to post-implementation reviews.

***Question 6:** Does your jurisdiction have requirements or guidance specific to audits of CIVs/pension funds from an auditor independence perspective? If yes, are those requirements included in audit-specific or CIV-specific regulation?*

We defer to the regulators/standard setters in the jurisdictions to respond to this question.