

**Discussion Group Session A—  
Exploring a Pathway to Convergence on the Concepts of PIE and ESPI**

**A. Background**

*Current Position in IESBA Code*

1. The concept of a public interest entity (PIE) is mainly referred to in the International Independence Standards (Part 4A of the Code) that apply to audits and reviews of financial statements. It is used to specify the applicability of certain independence requirements to audits and reviews of entities that are PIEs as defined in the Code.
2. The PIE concept was established in the Code in March 2008 when the IESBA finalized revisions to the independence provisions in the former Section 290. These revisions led to the present definition in the Code which is as follows:

Public interest entity	<ol style="list-style-type: none"> <li>(a) A listed entity; or</li> <li>(b) An entity:                             <ol style="list-style-type: none"> <li>(i) Defined by regulation or legislation as a public interest entity; or</li> <li>(ii) For which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation might be promulgated by any relevant regulator, including an audit regulator.</li> </ol> </li> </ol>
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3. The International Independence Standards also state the following in paragraph 400.8:
 

Some of the requirements and application material set out in this Part reflect the extent of public interest in certain entities which are defined to be public interest entities. Firms are encouraged to determine whether to treat additional entities, or certain categories of entities, as public interest entities because they have a large number and wide range of stakeholders. Factors to be considered include:

  - The nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders. Examples might include financial institutions, such as banks and insurance companies, and pension funds.
  - Size.
  - Number of employees.
4. In developing the concept of a PIE, the IESBA’s motivation was to recognize the need for more specific guidance on the application of the independence requirements to audits of entities of public interest than existed in the Code then. In addition, given the public interest associated with a wide range of entities, the IESBA sought to strengthen the Code by extending the listed entity independence provisions to all “entities of significant public interest.”
5. Appendix 1 summarizes the IESBA’s deliberations in arriving at the concept of a PIE and the related definition and guidance.

*Current Position in IAASB Standards*

6. The term “entity of significant public interest” (ESPI) was introduced in the ISAs to address a need that was expressed by certain stakeholders that some requirements in the ISAs that are designed to apply to listed entities should be extended to include ‘other entities’. It was possible to accommodate this need by initially aligning the ISAs with the IESBA Code of Ethics at the time (around 2005–2007). In this way, the auditor would be alerted that it may be appropriate to apply a requirement that was designed for an audit of a listed entity, to a broader range of entities.
7. The approach of the IAASB in relation to the use of the term ESPI recognizes that certain entities other than listed entities could have characteristics that give rise to similar public interest issues as listed entities. This pertains to the consideration of entities that have a large number and wide range of stakeholders, and the nature and size of the business. Various examples are included in application material to illustrate the types of entities that may exhibit such characteristics.
8. The rationale for using the term ESPI rather than PIE is primarily that ‘PIE’ remains difficult to interpret and apply, since it is very much a matter of jurisdictional definition and this could vary widely between jurisdictions. In certain instances, small or non-complex entities could be scoped into the definition of a PIE as used by a regulator or in legislation, for which the application of a requirement that has been designed to apply to listed entities (or entities similar in their nature and characteristics) would be considered impracticable or overly burdensome.
9. Appendix 2 summarizes the use of the term ESPI in the current IAASB Handbook as well as recent IAASB exposure drafts (EDs), and the reasoning for its use.

**B. Action Requested**

10. Participants are asked to discuss the following matters:
  - (a) What is the core issue?
  - (b) Where is commonality?
  - (c) What might be possible paths to convergence, and how might the two Boards’ standards evolve as a result?

## Development of Concept of Public Interest Entity in IESBA Code

### *December 2006 Exposure Draft*

1. In its December 2006 Exposure Draft of proposed revisions to the independence provisions in the former Section 290 of the Code, the IESBA proposed the following provisions:

290.22 Evaluating the significance of threats to independence and the safeguards necessary to eliminate them or reduce them to an acceptable level takes into account the extent of public interest in the entity. Entities of significant public interest are listed entities and certain other entities that, because of their business, size or number of employees, have a large number and wide range of stakeholders. The extent of the public interest in these entities is significant. This section, therefore, contains enhanced safeguards to recognize that interest.

290.23 In some countries, the entities considered to be of significant public interest for the purpose of determining the independence requirements that apply in that country are defined by law or regulation. In such cases, that definition should be used in applying the requirements in this section. In the absence of such a definition, member bodies should determine the types of entities that are of significant public interest and, thus, subject to the enhanced safeguards referred to above. Entities of significant public interest will always include listed entities, and, depending on the facts and circumstances, will normally include regulated financial institutions such as banks and insurance companies, and may include pension funds, government-agencies, government-controlled entities and not-for-profit entities.

2. In developing guidance on which entities should be considered to be entities of significant public interest, the IESBA reviewed guidance and practice in other jurisdictions. That review indicated that there were similarities in approach, for example, including listed entities within the national definition of a public interest entity, and including certain other entities based on a size test. There were, however, significant differences in the application of a size test. Further, the IESBA noted that in some jurisdictions, entities considered to be of significant public interest for independence purposes were defined by law or regulation. In considering this information, the IESBA concluded that it would be impracticable to develop a single definition of an entity of significant public interest that would have global application and be suitable in all jurisdictions. Accordingly, in those jurisdictions where entities considered to be of significant public interest for independence purposes are defined by law or regulation, the IESBA concluded that this definition should be used in applying the requirements of proposed revised Section 290. In the absence of such a definition, the IESBA concluded that IFAC member bodies should determine the types of entities that are of significant public interest in their particular jurisdictions.
3. The IESBA also took the view that because of the significant public interest associated with listed entities, such entities should always be considered to be entities of significant public interest. For other entities, the ED contained some flexibility for each jurisdiction to determine, based on the facts and circumstances, which entities should be considered to be entities of significant public interest.
4. While the IESBA noted a presumption that regulated financial institutions would be considered to be entities of significant public interest, it recognized that in some jurisdictions, it was possible that certain regulated financial institutions would not have a large number and a wide range of stakeholders, and thus the extent of public interest in those entities would not be significant.

Conversely, the IESBA noted that some pension funds, government-agencies, government-controlled entities and not-for-profit entities may have a large number and wide range of stakeholders and should, therefore, be treated as entities of significant public interest.

*Analysis of Responses to ED and Final IESBA Determination*

5. While the majority of respondents either agreed with the proposal, or agreed in large part with it but with some suggestions for clarification, many respondents strongly disagreed with the proposal for differing reasons.
6. There were comments that while the ED stated that entities of significant public interest are entities that “because of their size or number of employees, have a large number and wide range of stakeholders,” the examples provided would not necessarily meet this overall characteristic. The respondents expressed concern that, irrespective of this overall characteristic, some may inappropriately interpret this as meaning that the nature of the business itself would be sufficient to determine whether an entity should be considered to be an entity of significant public interest. These respondents suggested that greater emphasis be given to either the size of the entity or the fact that it has a large number and wide range of stakeholders.
7. Other respondents provided the following feedback:
  - Some expressed concern that the examples would be viewed as tantamount to a rule.
  - Some respondents expressed concern that the proposal could lead to inconsistent application because of differing interpretations from jurisdiction to jurisdiction. Some further commented that this could be particularly problematic for entities of significant public interest whose operations cross jurisdictions.
  - Some respondents suggested that it would be useful to have some alignment with the definition provided by the International Accounting Standards Board (IASB) in its Exposure Draft at the time, *IFRS for Small and Medium Sized Entities*, which referred to holding assets in a fiduciary capacity for a broad group of outsiders.
  - There was a view that the definition of entities of significant public interest should be aligned with the EU definition which, inter alia, includes all regulated banks as public interest entities.
  - There was also a view that it would not be appropriate to include all listed entities as entities of significant public interest because, in some jurisdictions, there are many small listed entities and such small listed entities would not have a large number and wide range of stakeholders. It was further noted that such entities may not have the level of sophistication that is necessary to comply with reporting requirements without the assistance of the audit firm.
8. In considering the number and range of comments received on this matter, the IESBA was mindful of the need for clear guidance on the definition of an entity of significant public interest in order for the Code to be consistently applied.
9. The IESBA considered whether emphasizing the size of the entity, or providing more guidance on the size of the entity, would be sufficient to address the concerns expressed and whether this would be capable of consistent application. The IESBA concluded that, in light of the concerns expressed, providing greater emphasis on the size of the entity would not address the concern that the examples provided could be viewed as tantamount to a rule. The IESBA also noted that, as it had observed in

the explanatory memorandum to the ED, it would not be possible to provide specific quantitative guidelines that would be appropriate for global application.

10. The IESBA considered whether adopting the IASB definition of an entity with public accountability would address the concerns expressed. The IESBA came to the view that this would not address the concern that the nature of the business itself, irrespective of size, would result in the entity being categorized as an entity of public interest. The IESBA noted that this definition would likely include all banks and other financial institutions such as credit unions and insurance companies. The IESBA took the view that because such entities might be quite small in some jurisdictions, it would be inappropriate to adopt such a broad definition for a Code that establishes global independence standards.
11. The IESBA also concluded that the EU definition was also very broad and would not be appropriate for a global Code to be adopted by IFAC member bodies, particularly given the concern expressed that in some jurisdictions, regulated banks are not large and treating such banks as public interest entities could be detrimental to audit quality.
12. The IESBA considered the suggestion that there should be some flexibility so that small listed entities would not always be considered to be entities of significant public interest. The IESBA determined that it would not be appropriate to provide this flexibility. Listed entities, regardless of their size, are the result of an overt decision by their management to become listed in order to seek sources of capital from the capital markets. Management of those entities understood that becoming a listed entity brought with it additional responsibilities and requirements. The IESBA also noted that the extant Code at the time did not provide flexibility for small listed entities. It therefore concluded that this would continue to be appropriate.
13. The IESBA noted that much of the concern expressed related to the lack of specificity in the proposed guidance on determining whether an entity would be considered to be an entity of significant public interest. The IESBA concluded that this concern should be addressed by defining entities of significant public interest narrowly as listed entities and any entities deemed by regulation or legislation to be an entity of significant public interest. Other than for listed entities, this would leave the determination of whether an entity is of significant public interest to the relevant regulators in each jurisdiction.
14. The IESBA therefore concluded that it was appropriate to modify the definition to include listed entities and other entities that regulation or legislation has designated to be an entity of significant public interest or for which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities.
15. In addition, the IESBA concluded that (the now former) Section 290 should contain an encouragement for firms and IFAC member bodies to consider whether additional entities, or categories of entities, should be treated as entities of significant public interest for independence purposes in their jurisdictions, thus subjecting their auditors to the more stringent independence requirements. Factors that the IESBA determined to add as guidance for consideration included: the nature of the business, such as the holding of assets in a fiduciary capacity (for example, financial institutions) for a large number of stakeholders, size and number of employees.
16. The IESBA also concluded that, given the narrower definition, it was appropriate to refer to these entities as “Public Interest Entities” as opposed to “Entities of Significant Public Interest.”

## APPENDIX 2

### Section 1: ESPI as Used in the Current 2018 IAASB Handbook and Recent Exposure Drafts

1. Below are relevant extracts from the Handbook and EDs. The term ESPI and PIE have been highlighted (using green and yellow, respectively) in all extracts presented in this Appendix.

#### ISA 260 (Revised) and ISA 700 (Revised)

##### ISA 260 (Revised), Communication with Those Charged with Governance

###### Requirements

###### *Auditor Independence*

17. In the case of listed entities, the auditor shall communicate with those charged with governance:
  - (a) A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and
    - (i) All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, may reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor; and
    - (ii) The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level. (Ref: Para. A29–A32)

###### Application and Other Explanatory Material

###### *Auditor Independence (Ref: Para. 17)*

- A31. Relevant ethical requirements or law or regulation may also specify particular communications to those charged with governance in circumstances where breaches of independence requirements have been identified. For example, the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) requires the auditor to communicate with those charged with governance in writing about any breach and the action the firm has taken or proposes to take.
- A32. The communication requirements relating to auditor independence that apply in the case of listed entities may also be appropriate in the case of some other entities, including those that may be of significant public interest, for example, because they have a large number and wide range of stakeholders and considering the nature and size of the business. Examples of such entities may include financial institutions (such as banks, insurance companies, and pension funds), and other entities such as charities. On the other hand, there may be situations where communications regarding independence may not be relevant, for example, where all of those

charged with governance have been informed of relevant facts through their management activities. This is particularly likely where the entity is owner-managed, and the auditor's firm and network firms have little involvement with the entity beyond a financial statement audit.

## **ISA 700 (Revised), Forming an Opinion and Reporting on Financial Statements**

### **Requirements**

#### Key Audit Matters

31. When the auditor is otherwise required by law or regulation or decides to communicate key audit matters in the auditor's report, the auditor shall do so in accordance with ISA 701. (Ref: Para. A40–A42)

### **Application and Other Explanatory Material**

#### Key Audit Matters (Ref: Para. 31)

- A40. Law or regulation may require communication of key audit matters for audits of entities other than listed entities, for example, entities characterized in such law or regulation as public interest entities.
- A41. The auditor may also decide to communicate key audit matters for other entities, including those that may be of significant public interest, for example because they have a large number and wide range of stakeholders and considering the nature and size of the business. Examples of such entities may include financial institutions (such as banks, insurance companies, and pension funds), and other entities such as charities.

## **ED-ISQM 1**

### **ED-ISQM 1, Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Related Services Engagements**

#### **Introduction**

##### *Scalability*

5. This ISQM requires the firm to apply a risk-based approach in the design, implementation and operation of the system of quality management, taking into account:
- (a) The nature and circumstances of the firm, including whether it is part of a network or uses service providers; and (Ref: Para. A22)
  - (b) The nature and circumstances of the engagements performed by the firm, including the types of engagements performed by the firm and the types of entities for which such engagements are performed. (Ref: Para. A23)

Accordingly, the complexity and formality of firms' systems of quality management will vary. For example, a firm that performs different types of engagements for a wide variety of entities, including audits of financial statements of listed entities or entities that are of significant public

**interest**, will likely need to have a more complex and more formal system of quality management than a firm that performs only reviews of financial statements or compilation engagements.

## Requirements

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## Engagement Performance

37. In designing and implementing responses to address the quality risks identified and assessed by the firm relating to the engagement performance quality objectives, the firm shall include the following responses:

...

- (e) Establishing policies or procedures addressing engagement quality reviews in accordance with ISQM 2, and that require an engagement quality review for: (Ref: Para. A101–A107)
  - (i) Audits of financial statements of listed entities;
  - (ii) Audits of financial statements of **entities** that the firm determines are **of significant public interest**; and
  - (iii) Audits or other engagements for which:
    - a. An engagement quality review is required by law or regulation; or
    - b. The firm determines that an engagement quality review is an appropriate response to assessed quality risks, based on the reasons for the assessments given to those risks.

...

## Application and Other Explanatory Material

### System of Quality Management

A23. The nature and circumstances of the engagements performed by the firm may include consideration of matters such as:

- The types of engagements performed by the firm, for example, whether the firm performs only compilation engagements or performs a variety of engagements, including audits of financial statements.
- The types of entities for which such engagements are undertaken, for example, the industries in which the entities operate and whether the entities are owner-managed, listed or **of significant public interest**. An **entity** may be **of significant public interest** because it has a large number and wide range of stakeholders or due to the nature and size of its business.
- External factors, such as relevant professional standards and law or regulation

...

*Engagements Subject to an Engagement Quality Review (Ref: Para. 37(e))*

A101. The categories of engagements for which an engagement quality review is required are not mutually exclusive. For example, many listed entities may be considered to be of **significant public interest** based on the characteristics described in paragraph A102. In addition, law or regulation may require engagement quality reviews to be performed for certain types of entities (e.g., entities with public accountability as defined in certain jurisdictions) or may include different criteria or characteristics that firms may use in determining whether an entity is of **significant public interest**.

A102. In determining whether an **entity is of significant public interest**, the firm may take into account, for example, whether the entity has a large number and wide range of stakeholders, and the nature and size of the business. The firm also may consider the relative significance of factors such as these in the context of the jurisdiction or region in which the entity operates. **Entities** that the firm determines to be **of significant public interest** may include entities such as financial institutions (e.g. certain banks, insurance companies, and pension funds), and other entities such as certain not-for-profit organizations.

...

A105. In some cases, there may be no engagements for which an engagement quality review is required to be performed (e.g., when a firm does not perform audits of listed entities or **entities of significant public interest** and other responses to assessed quality risks are determined by the firm to be appropriate).

**Considerations Specific to Public Sector Audit Organizations**

A106. Public sector **entities** may be **of significant public interest** due to their size and complexity, the range of their stakeholders and the nature of the services they provide. Factors to consider in determining whether a public sector **entity is of significant public interest** may include whether the entity is a national, regional or local government, or whether an opinion is being expressed on the entire entity or only certain units. Other factors to consider may include whether the entity is a corporation that is state owned or in which the state has a controlling stake or a stake with significant influence. Larger public sector **entities** may be determined to be **of significant public interest** due to their social or economic influence on the community or region in which the entity operates.

**Section 2: Overview of Developments in the ISAs regarding the Term ESPI**

2. This section presents a summary of the history of the introduction and use of the term ESPI as follows: ISA 260 (Revised) going back to March 2005; ISA 700 (Revised) going back to June 2013; and ED-ISQM 1 that was issued in February 2019.

**ISA 260 (Revised)**

3. The relevant history in relation to ISA 260 (Revised) can be traced back to March 2005 when the IAASB issued an ED in relation to its project to address auditors' communication with those charged with governance. At that point ISA 260 and ED-260 made no reference to ESPI.

4. Based on the meeting materials where the board discussed the comments received on ED-260 the following revised paragraph was presented in the marked version of the December 2005 IAASB agenda papers:

[Note: Paragraph 49 requires that for listed entities the auditor makes certain disclosures regarding auditor independence to those charged with governance.]

51. The auditor considers whether the communications set out in paragraph 49 are also ~~appropriate~~ relevant in the case of ~~entities~~ that are not listed entities, particularly those that may be ~~of significant public interest~~ because, as a result of their business, their size or their corporate status, they have a wide range of stakeholders. Examples of such entities might include public sector entities, credit institutions, insurance companies, and pension funds. Communications regarding independence may ~~not~~ be ~~unnecessary~~ relevant, e.g., where all of those charged with governance have been informed of relevant facts through their management activities. This is particularly likely to be the case where the entity is owner-managed, and the auditor's firm and network firms have little involvement with the entity beyond ~~an annual~~ a financial statement audit.

5. The related issues paper provides the following by way of explanation for the additions in paragraph 51 of proposed ISA 260:

Auditor Independence Applicable Only to Listed Entities

11. The ED required listed entities to make certain disclosures to those charged with governance regarding independence (paragraph 49). Many respondents recommended that this requirement be widened to include other entities. The main suggestions were to include all public sector entities, all ~~public interest entities~~, or all entities.

12. This requirement was restricted to listed entities to be consistent with the IFAC Code of Ethics. The Code also notes:

*Certain ~~entities~~ may be ~~of significant public interest~~ because, as a result of their business, their size or their corporate status they have a wide range of stakeholders. Examples of such entities might include listed companies, credit institutions, insurance companies, and pension funds. Because of the strong public interest in the financial statements of listed entities, certain paragraphs in this section deal with additional matters that are relevant to the audit of listed entities. Consideration should be given to the application of the principles set out in this section in relation to the audit of listed entities to other audit clients that may be ~~of significant public interest~~.*

13. The Task Force notes that paragraph 51 ("The auditor considers whether the communications set out in paragraph 49 are also relevant in the case of entities that are not listed entities ...") contains a similar sentiment to the above quote from the Code.

6. The next development occurred when ISA 260 was revised as part of the IAASB's Clarity Project. Paragraph 51, above, was moved into the application material of the proposed clarified ISA 260. The board approved clarified ISA 260 at its meeting in September 2007, which included the following application material to the requirement that for listed entities, the auditor shall make certain disclosures regarding auditor independence to those charged with governance:

A23. The communication requirements relating to auditor independence that apply in the case of listed entities may also be relevant in the case of some other entities, particularly those that may be of significant public interest because, as a result of their business, their size or their corporate status, they have a wide range of stakeholders. Examples of entities that are not listed entities, but where communication of auditor independence may be appropriate, include public sector entities, credit institutions, insurance companies, and retirement benefit funds. On the other hand, there may be situations where communications regarding independence may not be relevant, for example, where all of those charged with governance have been informed of relevant facts through their management activities. This is particularly likely where the entity is owner-managed, and the auditor's firm and network firms have little involvement with the entity beyond a financial statement audit.

7. The reasoning for leaving this paragraph largely unchanged can be found in the related issues paper (see extract below).

#### G. Listed versus public interest entities

- G1. (Old) paragraph 15 requires communication of certain matters related to independence. It applies only in the case of listed entities. Basel, AASB, CEBS, IAIS, Mazars, and NZICA suggest that it should apply for "public interest" entities (consistent with proposed changes to the IFAC Code of Ethics); and the Provincial Auditor for Saskatchewan suggests that it should apply for all entities.
- G2. This issue was discussed by the IAASB at its April 2007 meeting in the context of the requirement of proposed ISQC 1 (Redrafted) that listed entities have an engagement quality control review, at which time it was agreed "that to extent the requirement for reviews beyond listed entities would not be appropriate as part of the clarity project, but would be considered again when changes to the Code as a result of the IESBA exposure draft have been finalized. A decision on the matter at that time would have the benefit of being informed by feedback received by the IESBA on its exposure draft."
- G3. The task force considers this same rationale should be applied in the case of (old) paragraph 15.

8. ISA 260 was again revised during the IAASB's new and revised auditor reporting project, with the new and revised standards being issued in January 2015. The changes reflected in ISA 260 (Revised) are only in relation to revisions to the auditor reporting standards in the 700-series. The section in ISA 260 (Revised) regarding auditor independence (the requirements and application material) was not affected, except for some language and structuring updates. However, the use of the term, ESPI, and the context in which it is used, did not change. Extracts of the currently effective standard, ISA 260 (Revised), have been included in Section 1 of this Appendix.

#### **ISA 700 (Revised)**

9. In December 2011 the IAASB approved a Project Proposal with regard to auditor reporting. The resulting new and revised auditor reporting standards were approved at the IAASB meeting in September 2014, including ISA 700 (Revised) and ISA 701 (and four other standards). Developments in relation to the use of the term ESPI are summarized in the paragraphs that follow.

10. The Task Force's initial analysis of the comments received on the Auditor Reporting EDs, as was presented at the March 2014 IAASB meeting, noted, amongst other matters, that most respondents supported the IAASB's proposal for key audit matters (KAM) to be limited to audits of financial statements of listed entities. However, two Monitoring Group respondents were of the view that the requirement should be expanded to PIEs, with suggestions for a definition of PIE.
11. The following is an extract of the changes that were proposed by the Task Force at the June 2014 IAASB meeting in responding to the need to consider options relating to audits for which KAM should be required, or may otherwise be applied voluntarily (i.e. beyond audits of listed entities):

30a. When the auditor of a complete set of general purpose financial statements of an entity other than a listed entity shall also apply proposed ISA 701 when the auditor:

- (a) is required by law or regulation to do so, regardless of the opinion expressed; and
- (b) Otherwise decides to communicate key audit matters and has not expressed an adverse opinion or disclaimed an opinion on the financial statements in the auditor's report or otherwise decides to do so, the auditor shall apply proposed ISA 701. (Ref: Para. A3041–A3143)

Key Audit Matters (Ref: Para. 30a)

A42. The communication requirements relating to key audit matters that apply in the case of listed entities may also be appropriate in the case of some other entities, particularly those that may be of significant public interest because they have a large number and wide range of stakeholders. Factors that may be relevant include:

- The nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders. Examples may include financial institutions, such as banks and insurance companies, and pension funds;
- Size; and
- Number of employees.

Law or regulation may define these types or other entities as public interest entities, and may require communication of key audit matters for these entities.

12. The above application material was further revised to the current paragraph A41 in ISA 700 (Revised), that was approved in September 2014 (see extracts earlier in this Appendix).

### **ED-ISQM 1**

13. The proposed new standard on quality management at the firm level includes several references to ESPI, for example, in describing factors in relation to the nature and circumstances of the engagements performed by the firm that may be considered in establishing the firm's system of quality management (par. A23) and in relation engagements subject to an engagement quality review (par. 37(e), A101-A107). Relevant extracts from ED-ISQM 1 have been included in Section 1 of this Appendix.
14. The rationale for including the term, ESPI, in the ED can be found in the explanatory memorandum that was issued with ED-ISQM 1.

**Explanatory Memorandum:**

59. The ITC proposed several enhancements to address engagement quality reviews, given the need to keep the standard fit for purpose and enhance support for exercising professional skepticism at the engagement level. Among the proposals, the IAASB explored whether the requirements for engagements that should be subject to an engagement quality review should be strengthened by requiring an engagement quality review for audits of entities other than listed entities. The ITC considered whether it would be appropriate to require an engagement quality review to be performed for audits of public interest entities (PIEs), as this term is used in the Code. However, the IAASB recognized in the ITC the difficulty of defining the term on a global basis, given the various definitions and interpretations across different jurisdictions.
60. Respondents to the ITC supported strengthening the requirement; however, there was not extensive support for requiring the performance of an engagement quality review for audits of PIEs. Respondents who did not support this proposal noted that the lack of a universal definition of PIEs could lead to inconsistent application in practice. Further, they noted that in many jurisdictions PIEs could include very small or non-complex entities (such as small charities) and performing an engagement quality review for audits of such entities would be overly burdensome.
61. However, the IAASB recognizes the need to enhance the scope of engagements subject to an engagement quality review, because there are audits of certain entities for which engagement quality reviews would be appropriate. These entities may include, for example, some entities operating in the public sector, and financial institutions such as certain banks, insurance companies and pension funds. Accordingly, paragraph 37(e)(ii) of ED-ISQM 1 includes a new requirement for the firm's policies or procedures to require an engagement quality review for audits of financial statements of entities that the firm determines are of significant public interest. ED-ISQM 1 also provides application material that describes the characteristics of such entities, to support firms in fulfilling this requirement. "Entities that are of significant public interest" is a term that is used elsewhere in the IAASB's standards, such as ISA 700 (Revised) and ISA 260 (Revised), to describe those entities that may have characteristics that give rise to similar public interest issues as listed entities. Although the IAASB has determined that this term continues to be suitable for its purposes, there may be questions as to how the term relates to "public interest entity" as defined in the Code. If respondents have views on this topic, it would be helpful for these views to be included in their responses to Question 11.
15. The Quality Management Task Forces are in the process of analyzing and deliberating the comments that have been received on public exposure. Certain key issues will be presented to the Board at its September 2019 meeting.