

# Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code

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*IESBA Final Pronouncement April 2022*

Aneica Boyd, 8 June 2022



# Current Public Interest Entity (PIE) Definition

IESBA Code - listed entities

Determination of other entities – local regulators or other authorities and firms were also encouraged to consider whether additional entities should be treated as PIEs, taking into account guidance provided in the Code.

Call for revision to definition of PIE for financial institutions – regulatory stakeholders (International Association of Insurance Supervisors and the Basel Committee on Banking Supervision)

Regulators in many jurisdictions do not have the power to set a definition - the International Organization of Securities Commissions

Various jurisdictions eg. EU, Australia and South Africa have also taken different or more specific approaches to defining or scoping the concept of a PIE for their local purposes.

# Current Public Interest Entity (PIE) Definition

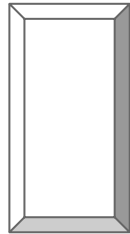
Small and medium practices (SMP) community, have expressed concern that the independence requirements in the Code are increasingly disproportionate in those circumstances where firms provide audit and review services to small entities that fall within the PIE definition.

The definition of “listed entity,” - some stakeholders have questioned the meaning of the term “recognized stock exchange” vs “regulated market” in the definition

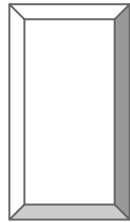
Developments in capital markets around the world and newer forms of capital raising such as crowd funding—and how these are regulated—have raised questions about the need to update the definition of a listed entity in the Code for clarity and continued relevance.

Principles-based approach to the definitions and avoiding an overly prescriptive approach that would undermine the Code’s global applicability.

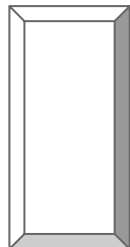
# IESBA PIE Project – 15 December 2024



To review, in coordination with the IAASB, the definitions of the terms “listed entity” and “PIE” in the Code with a view to revising them as necessary so that they remain relevant and fit for purpose; and



Establish agreement between the IESBA and IAASB on a common revised definition of the term “listed entity” that would be operable for both Boards’ standards; and



Develop a pathway that would achieve convergence between the concepts underpinning the definition of a PIE in the Code and the description of an entity of significant public interest (ESPI) in the IAASB standards to the greatest extent possible.





# IESBA Project Overview

**1** Introduce an overarching objective for additional independence requirements for audits of entities that are PIEs.

**2** Provide guidance on factors for consideration when determining the level of public interest in an entity.

**3** Expand the extant definition of PIE to a list of categories of entities that should be treated as PIEs, subject to refinement by the relevant local bodies responsible for ethics standard setting as part of the adoption and implementation process.

**4** Replace the term “listed entity” with one of the new PIE categories, “publicly traded entity.”

**5** Examine the role of the firm in context of the extant application material that encourages firms to determine whether to treat additional entities as PIEs and include enhanced guidance on factors for consideration by firms.

**6** Require firms to disclose if an audit client has applied PIE independence requirements



# Overarching objective – How should the definition be enhanced?

- Significant public interest in financial condition of certain entities
- There is heightened expectations from stakeholders regarding a firm's independence for PIE audits.
- As a result, additional independence requirements are necessary in areas such as fees, the provision of NAS, and long association in order to meet these heightened expectations.
- The International Independence Standard in Part 4A of the Code therefore contain two sets of independence requirements to meet the different expectations of stakeholders regarding a firm's independence depending on whether or not an entity is a PIE.
- These PIE and non-PIE independence requirements are designed to ensure auditors of any entity are independent both in mind and in appearance.

The IESBA believes it is important to make clear that these additional independence requirements are not about having a different “level” of independence (as all firms must be independent when performing an audit engagement) but rather about enhancing confidence in that independence.

IESBA used a more general term “financial condition” instead of narrower terms such as “financial statements,” “financial performance”.

# Overarching objective – How should the definition be enhanced?



## *Example 1*

Whilst there might be a significant level of public interest in the provision of services by a public hospital given its role within a jurisdiction's health services infrastructure, whether that public hospital should be categorized as a PIE in the local code will depend on the public interest in its financial condition. In this regard, the financial condition of a public hospital might not attract significant public interest if the government is committed to providing sufficient funding to enable it to continue the provision of its services.

## Non financial information

The IESBA maintained its view that given that the International Independence Standards within Part 4A of the Code deal only with audits and reviews of financial statements, the public interest in non-financial information should not form part of the overarching objective for additional independence requirements for the auditors of PIEs.

# Broad Approach to How the Code will be Applied

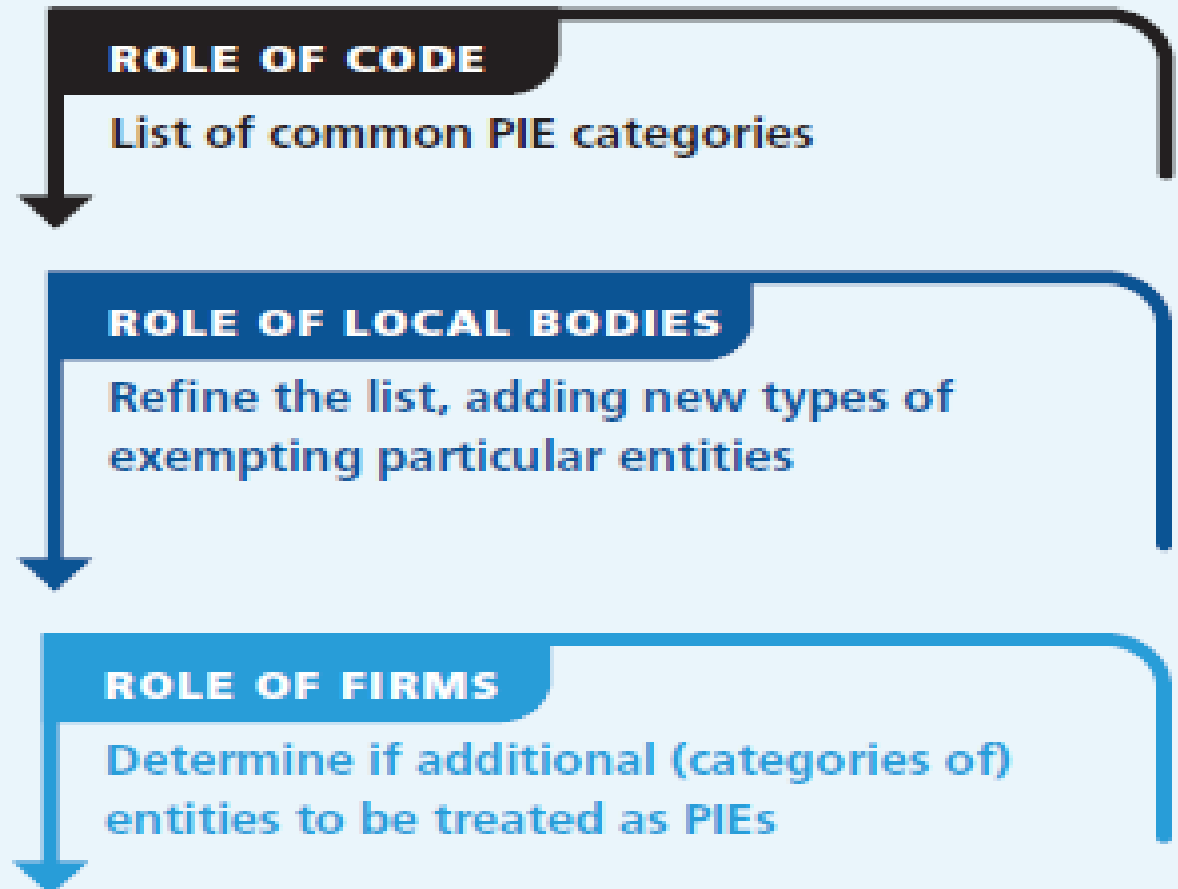
The development of a longer and broader list of high-level categories of entities as PIEs in the IESBA Code;

Refinement of the IESBA definition by relevant local bodies by tightening definitions, setting size criterion and adding new types of entities or exempting particular entities; and

Determination by firms if any additional entities should be treated as PIEs

## Broad Approach

A longer and more broadly defined list which local regulators and authorities can modify by following definitions, setting size criteria and adding new types of PIEs or exempting particular entities.





# Revised Public Interest Entity (PIE) Definition

Entities with deposit-taking and insurance businesses take on significant financial obligations to the public (both individuals and corporate entities) and, as a consequence of both taking on those obligations and the interconnectedness of the role they play in the financial markets, are generally subject to significant financial and prudential regulation and supervision.

The term “one of whose main functions” is used in order to **capture entities that have other main functions such as credit and lending** but also to **exclude those entities for which deposit-taking or insurance is not a main function**.

The exclusion of certain types of banks or insurance companies, for example credit unions or local mutual insurers is left to local jurisdictions during implementation.

- |                |  |
|----------------|--|
| (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  |
| <del>(d)</del> | <del>An entity whose function is to provide post-employment benefits</del>   |
| <del>(e)</del> | <del>An entity whose function is to act as a collective investment vehicle and which issues redeemable financial instruments to the public</del> |
| (f)            | An entity specified as such by law or regulation to meet the objective set in paragraph 400.9  |

5 specific categories

# Revised Public Interest Entity (PIE) Definition

The entities used to provide for post-employment benefits, such as pension funds, usually hold significant investments over the medium to longer term often on behalf of large numbers of stakeholders. There is, therefore, significant public interest in the financial condition of these entities. Some, but not all such entities, may also be regarded in the relevant jurisdictions as providing insurance-type benefits (such as annuities or medical insurance).

The suggestions are intended to capture both pension funds available to the public and those that are restricted to the employees of specified entities.

The term “whose function” is used instead of “one of whose main functions” in order not to include all employers that just contractually provide post-employment benefits to their employees.

- |                |  |
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5 specific categories

# Revised Public Interest Entity (PIE) Definition

## INCLUDE:

Categories that are likely to be adopted by most jurisdictions

Categories suited for a global list because of the nature of their main functions

## EXCLUDE:

Categories that would only be included by local bodies because they are very large

(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
<del>(d)</del>	<del>An entity whose function is to provide post-employment benefits</del>
<del>(e)</del>	<del>An entity whose function is to act as a collective investment vehicle and which issues redeemable financial instruments to the public</del>
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5 specific categories

# Revised Public Interest Entity (PIE) Definition

## Other categories

- Pension funds
- Collective investment vehicles
- Public utilities

- Private entities with large numbers of stakeholders (other than investors).
- Not-for-profit organizations or governmental entities.



# Refinement of Revised PIE Definition – Role of Local Body

Whether entities whose financial instruments are traded on a particular **second-tier market or other public forum** should be excluded?

Whether **smaller companies** should be excluded from any or all of the categories of PIE and what threshold should be set taking into account the **need to balance the public interest and the burden of additional requirements** imposed on the auditors of PIEs?

Whether certain types of financial institutions such as **credit unions or other mutual societies** should be excluded?

What types of **specialized insurance entities**, such as reinsurers, mutual captives or health insurers should be captured?

What types of **post-employment benefits**, for example one-off or regular pensions payments, defined benefit or defined contribution plans or medical benefits, should be excluded?

Whether there are other entities that are outside the IESBA's PIE categories but whose size or nature of operations might attract significant public interest in the event of financial failure, such as **large private or public sector companies, large private sector utilities or charities** providing services to a large number of beneficiaries or raising significant funds from the public?

For **private entities** should we use revenue thresholds or number of employees etc.?





# Factors for consideration in determining level of public interest

**1** Nature of an entity's business or activities and covers those entities that take on financial obligations to the public as a key element of their business model

**2** An entity is subject to financial or prudential regulatory supervision eg. financial services, but it is not intended to be restricted to such entities.

**3** Size of an entity and is of particular importance when a relevant local body is determining if there should be a size threshold to any of its categories of PIEs at the local level.

**4** The impact of an entity on the sector in which it operates. This factor includes consideration of how easily replaceable the entity is in the event of financial failure and hence whether such failure will cause significant disruption to the supply of goods or services on which the public may depend

**5** Direct impact on an entity's stakeholders

**6** Indirect impact that the entity might have on the overall economic system.





# Revised PIE Definition – Replacement of “listed” entity with “publicly traded” entity

Expanded the scope to more entities as it is not confined to shares, stock or debt traded only in **formal exchanges but also encompasses those in second-tier markets or over-the-counter trading platforms.**

The new term also aims to remove the confusion created by the term “recognized stock exchange” in the extant definition of listed entity.

The term “**financial instruments**” is intended to be broadly applied, covering “shares, stock or debt” (the term currently used in the extant definition of “listed entity”), securities, equity or debt instruments or other types of instruments such as warrants or hybrid securities.

Some financial instruments might only be listed and are not intended to be traded.

The IESBA is therefore of the view **that entities whose financial instruments are only listed or issued to the public with no trading do not necessarily attract significant public interest in their financial condition.**

The question was raised as to whether entities that raise funds through **initial coin offerings (ICOs)** should also be regarded as PIEs. Concluded to not include in the final pronouncement but acknowledged that some entities raising funds through new forms of capital might already meet the definition of a publicly traded entity



# Revised PIE Definition – Role of Firms

The third component of the IESBA's approach relates to an increased role for the firms and is made up of two new proposed requirements:

Elevation of extant application material to a **requirement for firms to determine if any additional entities** should be treated as PIEs. This was reverted from being a requirement to firms being encouraged to use application material for determination of such entities.

A new **requirement for the firms relating to increasing the transparency** of when an entity has been treated as a PIE.

The revision also require firms, in making such determination, to apply the reasonable and informed **third party test used to evaluate a self-review threat created by providing a non-assurance service to an audit client that is a public interest entity.**

## Scope -

It is not anticipated that a firm should treat an entity as a PIE when it has been **explicitly specified as not being a PIE by law or regulation.**

Should include those **entities that are in the process of being traded publicly**, similar to how this is approached in the definition of a “public accountability” entity in the International Financial Reporting Standard (IFRS) for Small and Medium-sized Entities (SMEs).

These two new factors are intended to cover the situations where in similar circumstances a firm or a predecessor firm has treated the same entity as a PIE, and where in similar circumstances the firm has treated other entities as PIEs. It is designed to reinforce consistency and mitigate against an entity switching auditors simply to achieve a different treatment.





# Revised PIE Definition – Role of Firms

## Scope -

A client or other relevant stakeholders such as a major shareholder might **ask for the entity to be treated as a PIE in order to enhance the confidence in its audit and its financial statements**. However, any such requests must be properly considered by the firm as the decision to treat additional entities as PIEs **ultimately rests with the firm**, taking into account the views of those charged with governance (TCWG) or the entity's stakeholders.

The IESBA is conscious that many of the additional independence requirements for PIE audits relate to **increased communication with TCWG**. Implicit in those requirements is that TCWG will respond appropriately which, in turn, relies on the entity having **an appropriate governance framework**.

In considering therefore whether to treat an additional entity as PIE, it is appropriate to take into account factors such as whether the entity has the necessary governance arrangements and whether its financial statements are subject to an appropriate level of accounting and financial reporting requirements.



# Revised PIE Definition – Auditors’ Report

## *Transparency Requirement*

Firms should disclose whether PIE independence requirements have been applied in performing an audit of the financial statements of an entity.

The disclosure should be made in “a manner deemed appropriate taking into account the timing and accessibility of the information to stakeholders.”

Allow for an exemption to the transparency requirement if making the disclosure would result in disclosing confidential future plans of the entity

## **IAASB ONGOING CONSIDERATIONS**

In November 2020, the IAASB considered three options with respect to requiring auditors to disclose in the auditor’s report that a client was treated as a PIE

Option 1 – No change to the auditor’s report

Option 2 – IAASB to pursue the possibility of enhanced transparency as part of its Auditor Reporting Post-Implementation Review (PIR)

Option 3 – IAASB to explore potential revisions to ISA 700.28(c).12F13 As part of its consideration, the IAASB also reviewed two illustrated drafts.



# Revised PIE Definition – Auditors’ Report

## *Transparency Requirement*

Whilst there was some support for Options 1 and 3, the majority of the IAASB members preferred Option 2 on the basis that further analysis as part of IAASB’s Auditor Reporting PIR will allow the Board to properly consider any potential impact and unintended consequences for auditor reporting, before deciding on an appropriate course of action. This also will provide an opportunity to further explore potential revisions such as those that were presented to the IAASB in November 2020 as part of Option 3.

Based on mixed feedback received from comments on the IESBA project the IAASB will continue its due process to determine whether the auditor’s report is a suitable location for such disclosure and, if so, how this may be accomplished.

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# Revised PIE Definition – Identifying related parties

## Definition of audit client in identifying related parties -

When an audit client is a **listed entity**, reference to audit client will always include all of its related entities (upstream, downstream and sister entities).

When an audit client **is not a listed entity**, references to an audit client includes those related entities over which the client has direct or indirect control (downstream only).

**Revised Code has replaced “listed entity” with “publicly traded entity”.**

Acknowledged the complexity of the issue and agreed that further research on this topic, including the nature of the ownership structures of eg private equity companies, is warranted in order that it can **gain a better understanding of the ramifications of extending the whole universe of related entities for listed entities to apply to all PIEs.**

The IESBA will consider a review of the definition of audit client as a potential future work stream as part of the development of its next Strategy and Work Plan for the period of 2024-2027



# IAASB Standards - Use of “Listed Entity” vs “PIE”

The term “**listed entity**” in ISAs and the International Standards on Quality Management (ISQMs) shares the same definition as that of the extant Code.

Currently, listed entity is the only class of entities that are subject to differential requirements with respect to the audits of their financial statements.

The term “public interest entity” is not used in the IAASB Standards. Instead, the term “**entity of significant public interest**” was introduced into the ISAs in response to the views of some stakeholders that it may be appropriate for some requirements in the ISAs that are designed to apply to listed entities to apply also to certain ‘other entities’.

It is understood that the IAASB’s rationale for not using the term PIE was primarily because of the concern that the term remains difficult to interpret and apply, since it is very much a matter of jurisdictional definition and this could vary widely between jurisdictions.



# IAASB Standards - Use of “Listed Entity” vs “PIE”

In March 2022, the IAASB plans to approve a project proposal to undertake targeted revisions to the ISQMs and ISAs.

Aspects of the IAASB project impacting the IESBA PIE project is expected to be finalized in line with the effective date of the revision 15 December 2024.

Preliminary views on incorporate the term “PIE” into its Standards:

There was strong support for a case-by-case approach when determining whether differential requirements already established within its Standards should be applied only to listed entities or more broadly to other categories of PIEs.

The IAASB needs to **assess the impact of expanding the differential requirements to all PIEs**, taking into account the rationale for applying these requirements to listed entities in its current Standards.

Upon review, the IAASB may **conclude that differential requirements relating to the audit may be appropriate for a subset of PIEs, such as listed entities, instead of all categories of PIEs.**



# What's Next?

- Continued dialogue between the ICAJ through the Audit Practice Committee and PAB
- Continued sensitization of the stakeholders within the industry
- Firms to start internal discussions on how policies and procedures will be adjusted and updated
- Small and medium size firms to consider specific nuances related to their practices for dialogue with the ICAJ and PAB
- Encourage stakeholders to share thoughts and comments on any other matter relating to the revision as soon as possible for consideration when the refinement process commences at the local level





# Thank you

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