

BRIEFING MEMO: IESBA CAG – PART I

September 11, 2023

Hybrid Meeting

Disclaimer: This memo is prepared by PIOB staff, in advance of the SSB/CAG meeting, applying their best knowledge and their own judgement in identifying and communicating matters of public interest and due process. PIOB Staff views are discussed with the PIOB observer and the PIOB Board and do not pre-empt further PIOB's views or discussions. The main objectives of this memo are to support the PIOB member in his/her SSB/CAG meeting observation and to help maintaining consistency and continuity of oversight.

The Agenda includes the following topics:

- B – SUSTAINABILITY WS2
- C – SUSTAINABILITY WS1
- E – USE OF EXPERTS

(The following agenda items will be covered in the BM - Part II: D – TAX PLANNING; F – STRATEGY AND WORK PLAN (SWP))

B - ETHICS (WORK STREAM 2)

Objective/scope, Background and Status: the Sustainability WG was established in March 2022 and the project proposal was approved in December 2022. The Sustainability work was split in three workstreams: two workstreams within Sustainability (profession-agnostic independence standards for sustainability assurance (workstream 1) and ethics standards for sustainability reporting and assurance (workstream 2); and one separate project for the Use of Experts.

Notes/key points from the review of the documentation for this meeting

The CAG will be provided with a report-back (item B) and a presentation (item B-1) on the approach and key aspects of the drafted ethics standards for sustainability

reporting¹ and assurance (WS2). The drafted standards (not provided in the documentation for the CAG) will be presented and discussed by the IESBA at its September meeting, while the ED is expected to be approved at its December 2023 meeting.

The main aspects of the TF's proposals are as follows:

- Scope of the standards: ethics standards for sustainability reporting will be applicable to PAs only; ethics standards for sustainability assurance will be applicable to PAs and non-PAs. The IESBA intends to “encourage” all preparers (PAs and non-PAs) of financial and non-financial information to use the Code.
 - The proposed scope of ethics standards for assurance engagements will cover (option 2 recommended by the TF)²: all sustainability assurance engagements and other services provided by sustainability assurance practitioners to the same clients. The rationale to include other services is that, if the fundamental principles in the Code are not applied for those services, there may be a negative impact on the credibility and trust of the sustainability assurance engagement.
- Communicating NOCLAR: given the current regime in Section 360, which does not require the auditor of financial statements (FS) to communicate NOCLAR to other PAs but requires the PAs providing other services to communicate to the auditor of the FS, the TF is proposing to reinforce the requirements. The auditor of FS would be required to communicate NOCLAR to the sustainability assurance practitioner (SAP), while the SAP would be required to communicate to the auditor of FS. NOCLAR in sustainability would be relevant and may have financial materiality and impact as well.
- Revised definition of “sustainability information”: while considering the definitions of different standard setters (e.g. ISSB, EFRAG, GRI, IAASB), the TF has revised the term “sustainability information”, which is a comprehensive one and includes, for example, the reference to historical and forward-looking information, to ESG and other sustainability factors, to impacts and double materiality, to the value chain, to the quantitative and qualitative aspects. The proposed definition is very similar to the “sustainability matters” definition used by the IAASB in ISSA 5000 (currently under exposure).

Public Interest Issues

Please refer to the latest PIOB PI Issues as of June, published in the PIOB website:
[IESBA Public Interest Issues](#)

¹ Limited to professional accountants only. The IESBA will explore, in the future, whether to expand ethics standards for sustainability reporting to all preparers (also non-professional accountants).

² Summary of recommendations for WS2, in terms of scope, are in slide # 22 of agenda item B-1.

PIOB Staff comments on PI

Since the June proposal, the TF has progressed its work. It has eliminated the reference to “heightened public interest” in the scope of the ethics standards for reporting and assurance engagements. This is in line with the suggestions, also provided by the PIOB, and the discussions at that meeting.

Clarity of the scope and consistency with WS1 is very important, though the provisions have a different objective and are addressed to different targets (in WS1 the independence provisions will apply to all assurance practitioners, both PAs and non-PAs). The ethics standards drafted by the WS2 will be split and addressed to different targets. Though the rationale for not extending ethics standards to all preparers has been discussed in previous occasions and adequately justified (e.g. no regulatory call, lack of relevant demand as an outcome of the roundtables held), it may cause some confusion on the application of the Code. We need to take into account that the independence standards (WS1) have a different scope and criteria to be met, and therefore create different layers of application, which may be confusing. Clarity and simplification in the scope is key, also taking into account the PIF qualitative characteristics which should be met.

It is therefore essential that the IESBA communicates in a clear way, especially to non-PAs, which parts of the Code apply to whom.

The IESBA plans encouraging voluntary use of the Code also to non-PAs for what concerns sustainability reporting. That would have a public interest impact, as all preparers would abide by the same requirements and rules. However, potential new work on that is currently postponed.

The proposals to strengthen communication around NOCLAR are welcome and demonstrate how intertwined audits of FS are with sustainability assurance engagements. When considering integrated reporting, that relation is even more significant.

The revised definition of “sustainability information” has been enhanced and has many similarities, in terms of elements included, with the “sustainability matters” definition in ISSA 5000. We reiterate that it is crucial for both SSBs to have aligned and consistent terms and definition. This is a process, and we recognize the ongoing coordination of the two SSBs, which should lead to such alignment and consistency by the time the two sets of standards are finalized.

Coordination among WS1 and WS2, as well as with the Use of Expert workstream, and with the IAASB is ongoing and needs to continue even during the exposure period of the standards.

The CAG will need to provide its input, though this is its last meeting, before it is replaced by the SAC. The discussions at the IESBA meeting will need to take into account this input and the draft of the standards will need to be further advanced to meet the approval of the ED, expected in December.

C - INDEPENDENCE (WORK STREAM 1)

Objective/scope, Background and Status: (see text in item B).

Notes/key points from the review of the documentation for this meeting

The CAG will be provided with a report-back (item C-2) and a presentation (item C-1) on the approach and main aspects of the drafted independence standards for sustainability assurance (WS1). The drafted standards (not provided in the documentation for the CAG) will be presented and discussed by the IESBA at its September meeting, while the ED is expected to be approved at its December 2023 meeting.

The main aspects of the TF's proposals are as follows:

- Scope of the standards: Part 5 will apply to assurance engagements (not to “certification” engagements), both to limited and reasonable assurance. Provisions in Part 5 will be equivalent to the provisions in Part 4A (independence in audits of financial statements). The reference to “heightened public interest” (presented in the first draft in June by the IESBA) has been deleted, while the criteria for the applicability of Part 5 have been maintained (i.e. sustainability information reported according to a general-purpose framework; required according to law or regulation; publicly disclosed to support investors and other stakeholders decision). For all other engagements, Part 4B will apply. The scope of the provisions is summarized in slide # 5 of item C-2.
- Quality Management System: a system of QMS, with requirements at least as demanding as in ISQM1, will have to be applied by the sustainability assurance practitioner (SAP) and its firm. This is consistent with ISSA 5000.
- PIE definition: Part 5 will differentiate requirements depending on the entity being a PIE or not (in line with Part 4A). Entities considered PIEs for the purposes of audits of financial statements, will also be considered PIEs for the purposes of sustainability assurance engagements.
- Providing NAS to sustainability assurance clients: current provisions and prohibitions of NAS in section 400 and 600 will apply also to sustainability assurance engagements. Given the context of sustainability, some NAS prohibitions need to be adapted (e.g. instead of “accounting and bookkeeping”, the reference will be to “sustainability data and information”).
- Group sustainability assurance engagements: Part 5 addresses independence of groups in sustainability assurance, as well as the use of work of other

practitioners (not part of the engagement team). The TF is addressing the situations where other practitioners cannot be subject to direction, supervision and review of the group firm. In these cases, the firm needs to obtain confirmation of the practitioner's independence from the entity on which an opinion on the sustainability information is obtained. In case confirmation of independence cannot be obtained, the work of the practitioner cannot be used.

- Relationship with value chain entities: the reporting boundary for sustainability information may be different from the reporting boundary of the FS (e.g. activities and resources which are up and down of the entity's value chain – suppliers, customers, etc.). There may be threats, which need to be addressed, in the relationship between the practitioner and the entities of the value chain (e.g. self-review threats, self-interest threats when there is a financial interest or a close business relationship).

Public Interest Issues

Please refer to the latest PIOB PI Issues as of June, published in the PIOB website:

[IESBA Public Interest Issues](#)

PIOB Staff comments on PI

Since the June proposal, the TF has progressed its work. As in WS2, WS1 has eliminated the reference to "heightened public interest" in the scope of the independence standards. This is in line with the suggestions, also provided by the PIOB, and the discussions at that meeting.

Clarity of the scope is essential, as the provisions drafted by WS1 are deemed to be applied by PAs and non-PAs, where the latter may not be familiar with the Code of Ethics. Compatibility with the scope of WS2 is also very important. As explained above, in WS2, there may be a question on whether there are too many layers, overlap or inconsistencies between the two scopes of the two workstreams. Specifically, one may ask whether the scope of Part 5 could be simplified, eliminating the "qualifiers". Could Part 5 be applied to all sustainability assurance engagements, without additional criteria to be met? This would achieve more clarity, one of the characteristics included in the PIF.

Additional NAS consideration and prohibition which may apply to sustainability assurance engagement are relevant. In June the TF had already considered the provisions of NAS in those situations, the relation to fees and fees dependency, as well as the rotation for partners/leaders involved in sustainability assurance engagements and in audits. The TF has been further working on these provisions and has considered

the need to adapt certain NAS in the context of sustainability engagement (vs. audits of FS).

The TF has included, in its proposals, independence required for group sustainability assurance engagements (for practitioners and firms), based on requirements in ISA 600, and recent changes in the Code. Though ISSA 5000 does not deal with group independence at the moment, this is an area which needs future coordination between the two SSBs. ISSA 5000 currently covers the use of experts and the responsibility of the practitioner when using the work of an expert. The two sets of standards will need to be consistent and aligned by the time they are finalized.

Lastly, consideration of the value chain and the possible threats which may arise when a practitioner has some relations with such entities in the value chain, is very welcome. Sustainability reporting will require additional effort from an entity's perspective, to gather information about its value chain and its resources upstream and downstream. Demands of assurance on this information will therefore increase and independence threats may also arise.

E – USE OF EXPERTS

Objective: to address ethics and independence considerations concerning the use of experts in the preparation, audit, and assurance of financial and sustainability information.

Background and Status: The IESBA approved a Project Proposal in December 2022, that will run in parallel with the two workstreams on Sustainability. The IESBA expects to approve an exposure draft (ED) in December 2023.

At the September 2023 CAG meeting, the task force (TF) will report back on March 2023 CAG feedback (item E-2), present feedback received on the use of experts from the roundtables (RT) on Sustainability held in March and April and will request input on proposed provisions.

Notes/key points from the review of the documentation for this meeting

The presentation (item E-1) provides a summary of key issues and the TF's proposals. Feedback from the roundtable can be accessed in IESBA's agenda item 5-A for the June 2023 meeting³.

The TF will present a summary of proposals that relate to the following:

³ Key issues are also described in PIOB's [BM for IESBA June Meeting 2023](#).

- Proposed Ethical Framework for external experts that include: definitions of “expert” and “expertise”; proposed provisions to clarify different roles of experts in Audit/assurance (consultation vs expert); evaluation of whether to use the work of an expert (based on expert’s competence, capability and objectivity); objectivity requirements applicable to external experts in audit or assurance engagements based on independence requirements of Part 4A or B of the Code; and guidance of factors to identify potential threats to the Fundamental Principles of the Code when using the work of an expert.
- Assessment of how the proposed framework meets selected PIF qualitative characteristics (comprehensiveness, scalability, clarity, implementability and enforceability).
- Challenges raised from using experts in emerging fields, that may make it difficult to evaluate competence or limit the availability of experts.

Public Interest Issues

Please refer to the PIOB’s Public Interest Issues, as of June 2023, published in the PIOB website:

[IESBA Public Interest Issues](#)

PIOB Staff comments on PI

The PIOB welcomed the responsiveness of IESBA to address ethical and independence considerations when using experts, both in the preparation and the assurance of information, including sustainability information. We also acknowledged that adequately addressing all aspects covered under this broad scope will raise several challenges.

As noted in our Public Interest Issues and the Briefing and Observation Memos for the June meeting, the proposed framework is responsive to the comments and concerns raised at the roundtables, while maintaining a focus on complying with the Code’s Conceptual Framework and providing a principles-based framework. However, the PIOB also has raised some concerns relating to:

- Definition of expert and consideration of the use of work of other practitioners (to be developed by the Sustainability project), since correctly determining which type of work is used in the engagement will determine applying independence rules or the “appropriateness framework” for experts. Coordination with the IESBA workstreams on Sustainability and with IAASB is essential.
- How to determine whether an individual is considered an expert (and subject to an evaluation of competence, capability and objectivity) vs. an individual

that provides a consultation (that would be subject to a significant influence test to determine whether they should be part of the AT and independent). Proposed provisions have been drafted to clarify the different roles. The provisions will be assessed in more detail as they are part of the IESBA meeting documentation.

- Whether the “objectivity” assessment (vs. requiring full independence) will meet expectations of users of audit/sustainability assurance reports, that are expected to be independent.

To address some of the challenges above, the PIOB suggested to integrate the assessment of the PIF characteristics when the TF evaluates the proposals considered and to guide them in reaching and supporting their conclusions. We should welcome the use of the PIF qualitative characteristics to assess the proposed framework. Some additional considerations to include in that assessment could be whether the proposals meet the expectations of users of audit or assurance reports (completeness through broad consultation, and relevance) and how the different/opposing characteristics have been balanced in the assessment performed.