

IESBA "Public Interest Entity" and "Listed Entity" Definitions (part 1)

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At its June 2020 virtual meeting, the International Ethics Standards Board for Accountants (IESBA or the Board) continued its deliberations on two key definitions in the *International Code of Ethics for Professional Accountant (including International Independence Standards) - Public Interest Entity (PIE) and Listed Entity*. This article provides highlights of the Agenda Item 8A, "[Definition of Listed Entity and Public Interest Entity - Issues and Task Force Views](#)".

Broadly, the project seeks to re-assess the definition of PIE for purposes of identifying a class of entities to which more restrictive auditor independence requirements would apply. For example: stricter independence requirements generally apply to nonassurance services (NAS), fees and partner rotation (long association). Proposals to further tighten rules in these areas (except partner rotation, which was significantly revised in 2017), are currently pending and will be the subject of future articles.

In March 2020, the task force and Board agreed on an approach to revise the [current PIE definition](#) by: expanding the categories of entities to be considered a PIE; anticipating that local regulators and oversight bodies would refine the list based on local preferences and circumstances; and requiring firms to determine whether to treat additional entities as PIEs when assessing independence. (Currently, firms are encouraged to do so.)

Recent outreach

The task force has sought views from the International Federation of Accountants (IFAC) Forum of Firms, National Standard Setters (NSS) and regulators from South Africa, Australia, Zambia and New Zealand. A meeting with the International Forum of Independent Audit Regulators (IFIAR) was held in May.

PIOB Public Interest Issues

An excerpt from the Agenda Item describes the Public Interest Oversight Board's (PIOB's) view:

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“In its April 2020 list of public interest issues on the IESBA work streams, the PIOB reaffirmed its view that it is crucial to determine the categories of entities (e.g. financial institutions, listed companies, significant utility companies), which should be subject to stricter provisions in the Code as the PIE definition affects other IESBA projects such as NAS and Fees. The PIOB noted that consideration should be given to any other entities that could pose a threat to financial stability. The PIOB also continued to highlight the importance of coordination between the IESBA and the IAASB to ensure consistent application of the two sets of standards.”

Overarching Objective

As noted in [Agenda Item 8B of the June 2020 meeting materials](#) (preliminary draft revisions), the PIE definition seeks to identify entities whose financial statement audits should be subject to more stringent independence standards, reflecting significant public interest in the financial condition of these entities. The *extent of public interest* would depend on factors such as:

1. nature of the business
2. size of the entity
3. importance of the entity to the markets
4. number and nature of stakeholders
5. potential systemic impact on other entities and the economy as a whole in the event of financial failure

As proposed, the purpose of these additional requirements and application material for PIEs is to enhance confidence in PIEs' financial statements by enhancing confidence in the *audits* of those financial statements.



Listed Entity

Listed Entity is currently defined as, “*An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.*” Issues the Board and task force have debated include:

- meaning of the term "recognized stock exchange," that is, whether is it the same as or broader than a "regulated market" (as used in the EU Directive)
- whether to clarify terms such as "publicly traded" and "public market"
- whether to include lightly regulated markets such as "over-the-counter" markets

Feedback from the Forum of Firm members suggested that those firms do not exclude any securities markets that are open to the public.

The task force's latest proposed definition for Listed Entity is: "*An entity whose shares, stock or debt are publicly traded*" which:

- removes the notion of a recognized stock exchange or regulated market, and
- would, according to NSS participants, include over-the-counter markets (e.g., entities listed on "pink sheets" in the US)

Preliminary Global List of PIE Categories

The task force has compiled the following preliminary global list of PIE categories:

- (a) An entity whose shares, stock or debts are publicly traded
- (b) An entity one of whose main functions is to take deposits from the public
- (c) An entity one of whose main functions is to provide insurance to the public
- (d) An entity whose function is to provide post-employment benefits
- (e) An entity that pools money from the public to purchase shares, stock and debts
- (f) An entity specified as such by law or regulation

The task force based the above list largely on the categories that several countries include in their national laws or regulations that define PIEs; the goal was to include categories accepted in most countries and exclude those accepted in only a very few. The task force would expect local bodies to tailor the scope of this list to identify PIEs in their own jurisdiction, for example, by excluding entities based on size or significance.

Concerns, Open Item and Rejected PIE Categories

Post-employment Benefits (item d above). Item d was the only item in the above list that was questioned with concerns expressed about the broadness of the category. However, the task force

regards the category to be appropriately included and noted that local regulators could consider the nature of the benefits provided and the structure and possibly, size of the entity.

Observation: In the US, the threshold for additional PIE independence rules are already established in law, e.g., employee benefit plans with over 100 participants are subject to Department of Labor (DOL) rules and those filing Form 11K must also comply with the Securities and Exchange Commission (SEC) independence rules.

Custodians as a possible addition to the list. Noting that national regulators have not generally identified these entities as PIEs, the task force has discussed but not yet reached a consensus on inclusion of entities that maintain assets on behalf of third-party clients.

Charities as a possible addition to the list. The task force rejected charities as an additional PIE category due the wide variety of charitable functions, operations and services. To illustrate this, the Agenda Item compared the Bill and Melinda Gates Foundation to the Red Cross. The former is one of the largest private foundations in the world but has a small number of donors and distributes its money to grantees rather than directly to benefit of the public. The latter runs programs that are funded by public donations and directly benefit persons at risk.

Observation: In the US, additional PIE independence rules apply under Government Accountability Office (Yellow Book) rules if the charity is audited under government auditing standards.

Public Utility Entities as a possible addition to the list. While public utilities provide essential services to the public, the level of public interest in these entities varies widely, thus the task force rejected this as an additional PIE category.

Observation: As noted in the Agenda Item, at the Board's March 2020 meeting, a question was raised as to whether the task force's proposal would capture entities such as public utilities and hospitals in which there is significant public interest. If broadly included as a PIE in the US, the impact would be quite significant as there are many thousands of such entities.

Public Sector Entities as a possible addition to the list. For reasons similar to public utilities, the task force rejected these entities as an additional PIE category. In addition, often these entities are audited by government employees, not professional accountants in public practice.

Observation: Like charities in the US, additional PIE independence rules apply under Government Accountability Office (Yellow Book) rules if the entity is audited under government auditing standards.

Large Private Companies as a possible addition to the list. Noting a global list will not be able to define what "large" means, the task force rejected these entities as an additional PIE category.

Private Equity Funds as a possible addition to the list. Since funds are raised privately from institutional investors, the task force rejected these entities as an additional PIE category.

Systemically Significant Entities (beyond financial institutions) as an additional category. The task force was unable to reach a consensus on other types of entities that would be “too big to fail”. The most frequently cited entities were major insurers and hedge funds/asset managers.

In June 2020, the Board further deliberated this list, which I will address in part 2 of this article.

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