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Dear Vita Ramanauskaite,

Response to the Accountancy Europe Discussion Paper (DP), *How to Respond to Assurance Needs on Non-Financial Information*

The European Federation of Accountants and Auditors for SMEs (“EFAA”) represents accountants and auditors providing professional services primarily to small and medium-sized entities (“SMEs”) both within the European Union and Europe as a whole. Constituents are mainly small practitioners (“SMPs”), including a significant number of sole practitioners. EFAA’s members, therefore, are SMEs themselves, and provide a range of professional services (e.g. audit, accounting, bookkeeping, tax and business advice) to SMEs. EFAA represents 17 national accounting, auditing and tax advisor organisations with more than 370,000 individual members.

EFAA commends Accountancy Europe (ACE) on this consultation which is both timely and thought provoking. Earlier this year we [responded](#) to a related consultation by the IAASB, their Discussion Paper (DP), [“Supporting Credibility and Trust in Emerging Forms of External Reporting: Ten Key Challenges for Assurance Engagements”](#). Many of the points we made then we reiterate here. EER, including that of reporting on non-financial information, are still evolving. We support the IAASB and ACE’s initiatives to better understand the developments and the challenges being encountered by professional service providers. We are pleased to provide our comments below, both ‘General Observations’ as well as comments on the questions posed as ‘Items for Discussion’ in the DP. As reporting on NFI by SMEs is limited – as confirmed by our ongoing investigation into the form and content of NFI by SMEs across countries with EFAA members - and assurance thereon rare our response is primarily limited to high-level points. These comments have been compiled by EFAA’s Assurance Expert Group. We look forward to further engagement on this issue with ACE.

General Observations

Role of Accountants and Assurance and Building Credibility and Trust

Considerable evidence, not least [Edelman’s Trust Barometer](#) indicates that trust in business, government, NGOs and media is declining. Accountants and their assurance services have a key role to play in helping rebuild credibility and trust especially in business.

NFI Reporting Requirements on SMEs

We are currently examining the nature and extent of NFI reporting by SMEs. While the EU Directive applies only to larger companies our preliminary findings reveal many countries have national

requirements for some type of NFI reporting by SMEs. The nature and extent of such reporting varies significantly from one country to another.

Demand for NFI Reporting and Assurance by SMEs

SMEs are closely woven into local communities. As such SMEs are typically interested in maintaining a positive community image that provides an impetus for social and environmental responsibility. More generally there is a growing demand for, and in turn assurance on, non-financial information, and a recognition that such information is as important as financial information in appraising the performance, position and prospects of an organisation. Some commentators, such as Baruch Lev, question whether the relevance of financial reporting given company value is increasingly driven by intangibles that fail to get recognised. The [IFAC paper](#) on environmental, social and governance (ESG) disclosures looks at this issue. Many SMEs are almost totally dependent on intangible assets and SME stakeholders are increasingly seeking non-financial information.

SMEs are generally motivated to report non-financial information to satisfy the demands of customers and providers of credit but are much less keen to do additional reporting where the source of the request is a government agency or regulator. One of the largest costs to SMEs, and some argue the second biggest barrier to innovation, is the cost of compliance with government red tape. It is necessary for SMEs to be convinced that the improved business performance – competitiveness, access to finance etc. - derived from providing better financial / non-financial information exceed the costs of preparation and assurance.

The drivers for reporting, and the assurance or other services thereon, by SMEs, especially those at the smaller end of the size spectrum, may differ from those of larger or medium-sized entities. Reporting and assurance for larger entities is often driven by the need to satisfy investors or meet government regulatory demands. The motivation for reporting for SMEs, especially the smaller owner-manager ones, is largely the desire to satisfy customers and improve business performance. For medium-sized businesses the motivation falls somewhere in between. Hence, in respect of Integrated Reporting (<IR>) SMEs are likely to be interested in the thinking it demands rather than the 'end of pipe' reporting and assurance or other service thereon. Medium-sized entities that have ambitions to grow and a desire to demonstrate that they can compete and be measured alongside larger entities may be more favorably inclined towards reporting.

SMEs, like SMPs, face intense resource constraints - time, knowledge, human resources and money. Three questions must be addressed for any change to have traction amongst SMEs - as follows, and in this order: what's in it for me; what will it cost me; and now, what is it? For many, if not most, SMEs the only reporting requirement is in relation to tax. SMEs are not likely to be receptive to providing reports that simply ends up on going to a government department or agency, which are often not held in high regard nor trusted. Standard setters and regulators like the European Commission and the IAASB need to be particularly sensitive to the cost-benefit considerations of NFI reporting by SMEs and assurance thereon.

While in the case of larger companies the demand for assurance on NFI will be primarily driven by external users for SMEs any demand is more likely to come from internal users, such as the business owner, customers, and the providers of finance such as banks. In Europe we predict that societal pressures will lead to more NFI assurance engagements being obtained voluntarily. Nevertheless, given the limited appetite right now for NFI reporting by SMEs, both in terms of market demand and regulatory reporting requirements, in the foreseeable future we see little demand or need for

assurance on NFI reporting by SMEs. We do, however, foresee SME NGOs increasingly being asked to provide assurance or AUP on NFI.

Scalability

In view of the acute cost-benefit concerns it's vital that standard setters like the IAASB keep proportionality / scalability front of mind as it goes about deciding the way forward. IFAC's [PPP8 on Enhanced Organizational Reporting](#) stresses the need for proportionality (page 4). This extends to assurance or other services on NFI reporting.

Standard setters and regulators also need to be alert to the risk of trickle-down whereby a requirement appropriate for and initially intended for larger entities and practices cascades down to SMEs and SMPs. Hence in thinking about the appropriate services, and the requirements for performing them, care needs to be taken to anticipate the possibility of such eventually getting imposed on SMEs and SMPs. There is some evidence of this happening with IFRS as [our research](#) testifies.

Integrated Thinking and Reporting

As mentioned above, EFAA believes there may be merit in SMEs, especially medium-sized businesses, pursuing integrated thinking, and a corresponding opportunity for SMPs to provide related business advisory services. We welcome the [IFAC publication "Creating Value for SMEs through Integrated Thinking"](#). Our director recently authored the article ["The Case for SMEs to Consider Integrated Thinking and Reporting"](#) posted to the IFAC Global Knowledge Gateway explaining why it might be suited to SMEs and what are the benefits, including facilitating access to finance (part two of the two part series to follow in early December).

Assurance Standards

Notwithstanding the above, most SMEs are required to report little if any NFI and their appetite to voluntarily supply NFI varies and depends on various factors including industry sector. Hence, EFAA sees little, if any, need for the IAASB's International Standards to extend to cover a broader range of engagements. While we believe it is too early to develop a subject-matter specific assurance engagement standard on NFI, there may be a case for additional guidance on how to use the existing standards on NFI engagements. EFAA also supports greater promotion of the scope, benefits and limitations of the IAASB's non-audit standards and monitoring their adoption and use.

Engaging SMEs

The SME sector comprises over 90% of business entities by number and accounts for most private sector employment, GDP and social and environmental impact. Hence, we encourage ACE to ensure sufficient outreach is undertaken with the SME sector, their representatives or those with expert knowledge of this sector. Liaison with [UEAPME](#) preferably in concert with EFAA would be most welcome. Standards and guidance for assurance on NFI needs to anticipate eventual application to SME engagements, be scalable and alert to the risk of trickle-down.

Specific Questions

The Basis: Professional Standards

Q1 What is your experience in applying available standards and guidance for NFI assurance, for example ISAE 3000? Have you come across challenges? Could you share some examples and practical solutions to those challenges?

Presently there is little need or demand amongst SMEs, especially those that are small informal owner-managed ones, for assurance or other professional services, or for further enhancement of the audit, to enhance credibility and trust when NFI is included in the annual report. Some SMEs may experience pressure to report on, and provide assurance, on NFI by large customers or by financiers. We are also witnessing an emerging demand from SMEs in some jurisdictions for an assurance readiness check or pre-assurance. In such cases clients usually perform a self-assessment or a gap-analysis and request an assurance report, typically limited assurance, for internal purposes. While the nature of the work performed by assurance providers is like an assurance engagement the assignment may also be considered an advisory service.

Perhaps the primary challenge is that of ensuring proportionality / scalability of the professional standards. We suspect the existing suit of standards and guidance for NFI assurance are not sufficiently scalable for them to be capable of cost effective use by SMPs on SME engagements. Hence, guidance on how such standards can be best applied in a proportional manner is welcome. Ultimately, for SMEs assurance, especially reasonable, may prove to be excessive with the costs exceeding the benefits. In the same way SMEs that are exempt from having to have an audit on their financial statements choose to have limited assurance or non-assurance like a compilation or AUP, if anything at all, on grounds of proportionality and cost we similarly foresee SMEs choosing something similar for their NFI. Furthermore, we do, however, foresee SME NGOs increasingly being asked to provide assurance or AUP on NFI. Therefore, international standard setters ought to focus, for now at least, on the development of guidance to assist practitioners in the proportional application of the requirements of limited assurance (review) or non-assurance International Standards (agreed-upon procedures (AUP) or compilation engagements). For example, compilation engagements for <IR> and AUP that an <IR> report uses the <IR> Framework.

Another challenge is that we suspect that market participants are insufficiently informed as to the types, characteristics and suitability of different types of professional services on NFI. Both professional service firms, or others, providing services and business and their stakeholders demanding / requesting services need to be sufficiently well informed as to what can be offered and the value of such offerings. As things stand many firms do not realize how they might leverage the existing standards and their expertise in this area and there's a corresponding lack of awareness amongst business and their stakeholders as to what firms can or could offer. We suspect this lack of awareness and understanding is most acute amongst SMEs and their advisors, SMPs included. Professional services are intended to enhance credibility and trust in reported NFI. It is vital that professional services directed at the SME sector are simple and low cost.

Step 1: Define the Scope of the Engagement

Q2 What is your experience in defining the scope of an assurance engagement? Have you come across any challenges? Could you share some examples and practical solutions to those challenges?

No comments. Please see remarks above.

Step 2: Assess the Subject Matter

Q3 What is your experience in assessing the subject matter for an assurance engagement? Have you come across any challenges? Could you share some examples and possible solution to the arising challenges?

No comments. Please see remarks above.

Step 3: Assess the Reporting Criteria

Q4 What is your experience in assessing the criteria? Have you come across any challenges? Could you share some examples and practical solutions to those challenges? What type of criteria might be considered not suitable?

We believe the plethora of reporting frameworks is a problem, especially for SMEs and their SMP accountants since they lack the expertise and resource to evaluate their suitability let alone use them. We also suspect that some of the frameworks are insufficiently scalable, having been developed with only larger companies and accounting firms in mind.

Step 4: Assess Materiality

Q5 What is your experience in performing a materiality assessment on NFI? Have you come across any challenges? Could you share some examples and possible solution to these challenges?

No comments. Please see remarks above.

Step 5: Consider Maturity of the Company's Reporting Processes

Q6 What is your experience when dealing with evolving reporting systems? Have you come across any challenges? Could you share some examples and practical solutions to these challenges?

The reporting systems of SMEs are typically simple. Technology, especially data analytics, is enhancing the sophistication and capability of the reporting systems of many SMEs. However, their systems are unlikely to share the inherent economies of scale that larger companies enjoy. Ultimately this means the identification, collation, and reporting of NFI by SMEs may not be as cost effective as larger entities.

Please see remarks above.

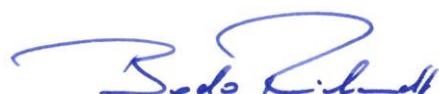
Step 6: Form of an Assurance Report

Q7 What is your experience in creating an assurance report? Have you come across challenges? Could you share some examples and practical solutions to those challenges?

No comments. Please see remarks above.

I trust that our comments above are clear. If you have any questions on our comments, please do not hesitate to contact me.

Yours faithfully,



Bodo Richardt

President