



Public Accountants and Auditors Board (PAAB)

Definition of Public Interest Entity (PIE)

DEFINITION OF PUBLIC INTEREST ENTITY

Public Interest Entities

Scope of this Pronouncement

1. The PAAB Pronouncement 2/2016 : **Definition of Public Interest Entity** provides a definition of Public Interest Entity that can be more consistently applied primarily among registered auditors and accountants as well as the general market in Zimbabwe ;
2. **Effective Date**
This effective date for this PAAB Pronouncement: Effective date for implementation of this guidance is for reports issued on or after 31 December 2016 with early adoption permitted.

Objective

3. In line with the IESBA Code, this proposed Pronouncement is premised on the principle that, in the case of audit engagements, it is in the public interest that members of the audit teams, firms and network firms are independent of audit clients. The Code, in Section 290, contains additional independence requirements that reflect the *extent* of public interest in certain entities (defined as Public Interest Entities).
4. This Pronouncement seeks to provide specific guidance which can be used to determine whether an entity is a Public Interest Entity or not.

Requirements

Entities that will satisfy the definition of Public Interest Entities are:

5. Listed Entities
6. Public Entities as defined by the Public Finance Management Act 22:19 and those required to be audited by the Auditor General under the Audit Office Act 22:18 as read together by the Constitution of Zimbabwe section 309
7. Entities carrying on banking activity as defined in the Banking Act 24:20 and building societies as defined in the Building Societies Act 24:02 and Asset Managers as defined by the Asset Management Act 24:26 and are required to be licensed under these Acts.
8. Insurers registered under Insurance Act 24:07

9. Collective Investment Schemes in terms of the Collective Investment Schemes Act, 24:19
10. Pension funds as required to be registered in terms of the Pension and Provident Funds Act 24:09 that are open to a large number and wide range of employees.
11. Medical Aid Societies as defined in the Medical Services Act 15:13
12. *Economically Significant Entities [PAAB is still consulting on appropriate thresholds for including Economically significant entities and will issue an amendment in due course.]*
13. Other issuers of debt and equity instruments to the public.

Responsibility of the Firm

The amendments introduced that relate to the classification of PIEs are not intended to be a complete list, but rather a list of entities that would normally be presumed to be PIEs. Thus, there may be entities that may be considered to be PIEs although they are not specifically included in this guide.

Responsibility of the Preparer

The PAAB has prescribed the signing convention for financial statements of all public interest entities to contain the full name, qualifications and PAAB registration number of the person charged with supervising the preparation of financial statements of public interest entities. This new signing convention does not take away the common law, Companies Act or other legislative or regulatory requirement for directors' or those charged with governance's responsibility for the financial statements. It is a separate and additional requirement.

Effective date for implementation of this guidance is for reports issued on or after 31 December 2016 with early adoption permitted.

Appendix 1: Explanatory Guidance (*This is not part of the Pronouncement but additional guidance that can be used and other consideration by the board in coming out with the proposed definition*)

The need to protect the Public Interest

- A1.1 The PAAB recognises that concerns raised by stakeholders about the appearance of independence, the protection of the public interest, and continued confidence and trust in the independence of the audit process are an important rationale for the proposed Pronouncement in this Exposure Draft.
- A1.2 The PAAB also recognises that the different approaches adopted by registered auditors and accountants when considering whether clients are Public Interest Entities results in materially different outcomes in the identification of those entities whose activities have a significant impact on the public interest. In its first round of inspections, PAAB has identified that certain registered auditors hold a narrow view on which clients fall within the Public Interest Entity definition, whereas other firms adopt a wider interpretation.
- A1.3 The proposed amendment is intended to enhance perceptions of the auditor's independence in mind and appearance especially relating to investor public interest where there are a large number and a wide range of stakeholders.

Consistently applied

- A1.4 The benefit of the proposed Zimbabwean definition is that it will ensure that certain entities would always be treated as *Public Interest Entities* to avoid the risk of different treatment amongst firms.
- A1.5 In the PAAB's view, this would enhance consistency between the increased regulatory supervision of entities in which there is a higher level of public interest and the more onerous independence requirements imposed on the auditors of such Public Interest Entities. As these entities are held to higher financial reporting and regulatory requirements, their auditors ought to be held to a higher independence requirement.

A1.6 The PAAB recognises that the issues are finely balanced and that any change must be seen by stakeholders as being substantive and made on a sound and defensible basis, while a balance is achieved between the cost and complexity of implementation and the benefits.

A1.7 The PAAB has carefully considered the stakeholder concerns which support strengthening the consistent application of the independence requirements applicable to Public Interest Entities. In doing so, it has kept in mind that the goal is to promote and enhance audit quality, objectivity and professional scepticism when performing audits and/or reviews of Public Interest Entities.

A1.8 The PAAB has taken into account the need for some flexibility and judgement when considering which entities are Public Interest Entities and decided that not including some flexibility and judgement may lead to unintended consequences.

Internationally comparable

A1.9 The IESBA Code in Section 290.26 encourages but does not require firms to consider other factors, such as the nature of business, size and number of employees, when determining whether entities are Public Interest Entities. Evidence gathered from PAAB inspections indicates that these criteria have not been consistently applied in Zimbabwe and that more definitive guidance is required. The IESBA clearly intended that the more restrictive independence requirements should apply to entities where an *important* public interest exists (i.e. not only Listed Entities). If the intention was to apply only to Listed Entities then 290.25 (a) of the definition would have been sufficient and it would not be necessary to have 290.25 (b). At the 2010 World Congress of Accountants the IESBA Chairman publicly stated that the definition of *Public Interest Entities* covers more than Listed Entities. As an example, he noted that the European Union (EU) definition captures banks and insurance companies in addition to listed companies.

A1.10 Before issuing this proposed amendment to the code, the PAAB considered the definition of *Public Interest Entity* taking into account existing and proposed definitions in several other jurisdictions. We considered the definition of Public Interest Entities from South Africa, European Union and Malaysia.

A1.11 Preparers, other regulators and users of financial statements can also use this guidance in their dealing with different entities, be it on risk assessment or on any other required assessment.

Significant Matters

A1.12 The significant matters to be considered as a result of applying this proposed Pronouncement can be broken down into:

- The firm's responsibility to consider if an audit or review client is a Public Interest Entity;
- The opportunity for a firm to consider the client not to be a Public Interest Entity and the requirement for the firm to document the reasons (the –rebuttable presumption); and
- The entities that are likely to be considered to be a Public Interest Entity.

The firm's responsibility

A1.13 The definition makes the rebuttable presumption that certain entities are likely to be Public Interest Entities. Where the audit firm does not agree that an audit client is a Public Interest Entity, even though it falls within the list of entities considered likely to be a Public Interest Entity, the firm is required to document its reasoning for the exception.

Entities that are likely to be considered to be a Public Interest Entity

A1.14 When considering which entities to include in the definition, the PAAB applied the concept of public accountability. Public accountability may be defined as accountability to those existing and potential resource providers and others external to the entity that make economic decisions but are not in a position to demand reports tailored to meet their particular information needs. Public accountability can arise either through the public holding debt or equity instruments in the entity or if the entity holds assets of the public in a fiduciary capacity.

A1.15 In addition, the PAAB also took into account the extent of public interest in an entity, using the factors set out in Section 290.26 of the Code, such as the number and range of stakeholders, the size of the entity and the amount of assets held in a fiduciary capacity.

A1.16 Based on these criteria, additional Public Interest Entities are likely to be large financial institutions and public sector organisations. If an entity has a large number and wide range of stakeholders that have a direct financial interest in the entity, then that entity was included in the list below.

A1.17 The PAAB has consulted with the Securities Exchange Commission, the ZSE, Reserve Bank of Zimbabwe, Insurance and Pension Commission and the Auditor – General in the preparation of

this exposure draft, and particularly with regard to the entities that fall within their jurisdiction and that, in their view, are likely to be considered to be Public Interest Entities. We are of the opinion that the size of an insurer, asset manager and deposit taking financial services provider is not relevant to consideration of whether those entities should be considered a Public Interest Entity in terms of paragraph 290.26 of the Code.

A1.18 The proposed lists the following entities as likely to be considered to be Public Interest Entities.

A1.19 Listed Entities

A1.20 Public Entities as defined by the Public Finance Management Act 22:19 and those required to be audited by the Auditor General under the Audit Office Act 22:18 as read together by the Constitution section 309

A1.21 Entities carrying on banking activity as defined in the Banking Act 24:20 and building societies as defined in the Building Societies Act 24:02 and Asset Managers as defined by the Asset Management Act 24:26 and are licensed under these acts.

A1.22 Insurers registered under Insurance Act 24:07

A1.23 Collective Investment Schemes in terms of the Collective Investment Schemes Act, 24:19

A1.24 Pension funds required to be registered under the Pension and Provident Funds Act 24:09 that are open to a large number and wide range of employees.

A1.25 Medical Aid Societies as defined in the Medical Services Act 15:13

A1.26 Economically Significant entities - PAAB is still consulting on the appropriate thresholds to be included on Economically significant entities and an amendment with include economically significant entities will be issued in due course.

A1.27 Other issuers of debt and equity instruments to the public.

We will discuss some of the entities mentioned above individually

A1.28 Public Entities as defined by the Public Finance Management Act 22:19. Section 2 of the Public Finance Management Act 22:19 defines public entities as :

‘(a) any corporate body established by or in terms of any Act for special purposes;

(b) any company in which the State has a controlling interest, whether by virtue of holding or controlling shares therein or by virtue of a right of appointment of

members to the controlling body thereof or otherwise, and includes any company which is a subsidiary, as determined in accordance with section 143 of the Companies Act [Chapter 24:03], of such a body;

(c) a local authority;

(d) any partnership or joint venture between the State and any person

A1.29 Public Entities also includes entities that are required to be audited by the Auditor General under the Audit Office Act 22:18 as read together with the constitution of Zimbabwe section 309

A1.30 Entities carrying on banking activity as defined in the Banking Act 24:20 and building societies as defined in the Building Societies Act 24:02 and Asset Managers as defined by the Asset Management Act 24:26

A1.31 Due to the nature of the work performed by banks, building societies and asset managers, which normally includes holding assets in fiduciary capacity for a large number of stakeholders and the use of those funds in credit lending activities, there are likely to be considered a Public Interest Entity.

A1.32 Insurers - Due to the significance of the —promise to pay obligations which both short and long term insurers generally have towards a large number and wide range of policy holders, insurers are considered likely to be Public Interest Entities.

A1.33 Pension Funds - By their very nature, funds that hold significant asset are likely to be open to a large number and wide range of members and would normally hold a large amount of funds in fiduciary capacity on behalf of a large number of stakeholders and are likely to be considered a Public Interest Entity.

A1.34 In contrast, smaller funds that are not open to the public, such as stand-alone employer funds, have not been included in this proposed amendment due to the limited number and narrow range of stakeholders.

A1.35 Medical aid societies - An open medical aid is one that is open to all Zimbabweans who can pay for the membership. Open medical aid schemes, by their nature, typically have significant —promise to pay obligations towards a large number and wide range of policy holders, and may also hold substantial policy holder funds in medical savings accounts. As a result, open medical aid schemes are considered likely to be Public Interest Entities.

A1.36 Other issuers of debt and equity instruments to the public - This category has been included to take into account other entities that are not listed on a regulated stock exchange, but may have a large number and wide range of financial stakeholders.

Analysis of overall impact of the proposed changes

Implication for the audit profession

A1.37 The proposed definition will promote and enhance audit quality, objectivity and professional skepticism in addressing the public perception related to threats to independence. This amendment will strengthen the independence requirements in the Code, thus strengthening the reputation of the auditing profession and the protection of the public

At a firm Level

A1.38 The proposed definition places an additional level of responsibility on the audit firms. They will be required to consider if an entity other than a listed entity is a Public Interest Entity. This includes the responsibility to properly motivate and document any decision to rebut the presumption that an individual entity is a Public Interest Entity in accordance with this Code.

At an Engagement Level

A1.39 Auditors who perform audit and review engagements for entities that are considered to be Public Interest Entities will have to consider the services that are prohibited and the additional independence requirements imposed by the Code specifically for Public Interest Entities, including those set out in the table below:

Code Paragraph	Prohibition or Independence requirement	Other
Paragraph 290.137	Prohibits a key audit partner or senior managing partner joining a Public Interest Entity client before a defined time out	

	period	
Paragraph 290.149	Prohibits a key audit partner serving more than 7 years on a Public Interest Entity client	The Banking Pronouncements has more stringent rotation requirements
Paragraph 290.177	Prohibits the provision of Valuation Services for an Audit Client	
Paragraph 290.183	Prohibits the preparation of calculation of current taxation and deferred taxation liabilities (assets)	
Paragraph 290.197	Prohibits the provision of Internal Audit Services, relating to internal controls over financial reporting, financial accounting systems or financial statements amounts disclosed to an audit client	
Paragraph 290.203	Prohibits the provision of services involving the design or implementation of an IT system	
Paragraph 290.212	Prohibits the provision of recruiting directors/officers, or senior management who will have significant influence over accounting records or financial	

	statements	
Paragraph 290.219	If in two consecutive years the total fee from one client is greater than the total fee earned by the firm, then dependency on the client needs to be considered	