First-Time Implementation Guide

The International Standard on Auditing of Financial Statement of Less Complex Entities (ISA for LCE)

IAASB
International Auditing and Assurance Standards Board
AN IFEA BOARD

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THE INTERNATIONAL STANDARD ON AUDITING FOR AUDITS OF FINANCIAL STATEMENTS OF LESS COMPLEX ENTITIES FIRST-TIME IMPLEMENTATION GUIDE

CONTENTS

This publication has been prepared by the Staff of the International Auditing and Assurance Standards Board (IAASB). The objective of this First-Time Implementation Guide is to help understand and apply the International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (the ISA for LCE). It does not constitute an authoritative pronouncement of the IAASB, nor does it amend or override the ISA for LCE, the text of which alone is authoritative. Further, this publication is not meant to be exhaustive, and any examples are provided for illustrative purposes only. Reading this publication is not a substitute for reading the ISA for LCE.

I. INTRODUCTION

In December 2023, the IAASB released its International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (the ISA for LCE). The ISA for LCE is a new IAASB standard for financial audits of less complex entities (LCE). It is a standalone standard which is proportionate and tailored to the needs of an audit of an LCE.

This icon is used throughout this guide to highlight references to specific paragraphs in the ISA for LCE.

The ISA for LCE was developed to provide a global solution to the growing concern about the length, complexity, and understandability of the International Standards on Auditing (ISA) and their application to audits of LCEs.

The ISA for LCE contains requirements that enable the auditor to obtain sufficient appropriate audit evidence that provides the basis for expressing a reasonable assurance opinion. Audits conducted in accordance with the ISA for LCE enhance the trust and confidence of users of financial statement of LCEs in making decisions. The ISA for LCE also promotes the consistent application of auditing standards to audits of LCEs and reduce the risk of jurisdictional divergence by driving consistency and comparability globally.

Adopting the ISA for LCE assists auditors to deliver effective high-quality audits for LCEs. Refer to the Adoption Guide for guidance on how to adopt the ISA for LCE.

What Does the ISA for LCE Address?

The ISA for LCE has been designed to achieve reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, for audits of financial statements of LCEs.

The ISA for LCE is written in the context of an audit of a complete set of a general purpose financial statements of an LCE. If the entity is an LCE as set out in Part A of the ISA for LCE, the standard may also be adapted as necessary in the circumstances of the engagement to:

- An audit of a complete set of special purpose financial statements; or
- An audit of a single financial statement or of a specific element, account or item of a financial statement.

The ISA for LCE applies to financial statements prepared in accordance with fair presentation frameworks and compliance frameworks.

II. EFFECTIVE DATE[1]

1.1.1

The ISA for LCE is effective for audits of financial statements of LCEs for periods beginning on or after December 15, 2025. Early adoption is permitted and encouraged.

III. OVERARCHING CONCEPTS IN THE ISA FOR LCE

P.3

1. Separate Standalone Standard

The ISA for LCE is a separate, standalone standard, designed to be proportionate to the typical nature and circumstances of an LCE. It is a “self-contained” standard that addresses the fundamental concepts and general principles that underpin an audit of financial statements, as well as all the stages of an audit engagement, from engagement acceptance through to auditor reporting.

The standalone nature of the ISA for LCE means that it does not require any other IAASB engagement standards to be applied with the ISA for LCE. Specifically, the standard is separate from the ISAs and there is no direct reference back to the requirements or application materials in the ISAs in its application. This means that if there is a circumstance that has not been contemplated in the design of the ISA for LCE as addressed in the Authority of the standard (Part A), relevant ISA requirements cannot be used to address the circumstance (i.e., to “top-up”).

For example, consider the circumstance where an entity has accounting estimates calculated using a bespoke, complex models that are not contemplated by the standard, but is otherwise an LCE. In this instance, an auditor cannot use the ISA for LCE together with requirements from ISA 540 (Revised)[2] to supplement what may not be addressed in the ISA for LCE when planning and performing the audit. Consequently, an auditor would then need to apply the ISAs or other appropriate auditing standards because the ISA for LCE, in its design, does not address complex matters or circumstances.

2. Reasonable Assurance

P.1

The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements of an entity. The auditor achieves this by expressing an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. As with the ISAs, when applying the ISA for LCE, the auditor plans and performs the audit to obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level in the circumstances of the engagement as a basis for the auditor’s opinion. The ISA for LCE contains requirements for the auditor to

[1] The ISA for LCE can only be used by an auditor when the standard is adopted in their jurisdiction.

[2] ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*

obtain sufficient appropriate audit evidence. Reasonable assurance, in the context of an audit of financial statements, is a high, but not absolute, level of assurance.

3. Overall Design of the ISA for LCE

The overall design principles of the ISA for LCE are set out below.

Risked Based Approach and Principle Based

As with the ISAs, the ISA for LCE utilizes a risk-based approach to an audit, with requirements that are principles-based. This enables the standard to be used across a wide variety of LCEs with a wide range of circumstances and across sectors or industries, taking into account the applicability of the standard as addressed in Part A of the ISA for LCE.

Proportionality

The requirements and Essential Explanatory Material (EEM) in the ISA for LCE are designed to be proportionate to the typical nature and circumstances of an audit of an LCE. Requirements and EEM that address complex matters or circumstances are excluded from the ISA for LCE.

It is not envisioned that the ISA for LCE will necessarily reduce the core procedures the auditor is required to perform to support the overall quality of the audit. There has been a strong message from the IAASB's stakeholders that the standard should be based on the ISAs, and retain the robustness of an audit performed using the ISAs. Accordingly, the ISA for LCE presents the requirements for an audit of an LCE based on the core requirements of the ISAs but drafted and presented in a more understandable and straightforward way, including that the requirements follow the flow of an audit engagement.

Intuitive Structure

The structure of the ISA for LCE follows the natural flow of the audit, from client acceptance or continuance to reporting. Section IV describes the structure of the standard in more detail.

Use of Core ISA Concepts

The core concepts used in the ISA for LCE are the same to those used in an ISA audit. For example, an audit performed under the ISA for LCE applies a risk-based approach and is underpinned by the auditor exercising professional judgement and professional skepticism.

Focused on Expected Outcome

The ISA for LCE focusses on what the outcome of the requirement is that the auditor needs to achieve. The requirements describe what the auditor needs to do without including unnecessary granularity. The requirements are expected to deliver a similar outcome as with the ISA requirements when applied to an audit of an LCE.

Clear, Understandable and Concise

The requirements in the ISA for LCE have been written to be clear, understandable and concise, avoiding any unnecessary words, repetition, or ambiguous language. In developing the ISA for LCE, the IAASB used the Complexity, Understandability, Scalability and Proportionality Drafting Principles and Guidelines.

Drafting Principles of the ISA for LCE

The IAASB aims to set high quality international standards that are understandable, clear and capable of consistent application, thereby serving to enhance the quality and uniformity of practice worldwide. This includes presenting any required actions as clear, understandable and stated as simply and concisely as practical. In the ISA for LCE, material that is educational or background in nature has not been included. In addition, the IAASB has focused on:

- Simpler numbering.
- Avoiding long or multiple layers of bullet lists, including limiting the number of “sub-bullets” where appropriate.
- One thought per paragraph.
- Combining requirements from the ISAs where appropriate and avoiding repetition.
- Articulating the requirements in a clearer and simpler way where feasible.

In addition, the IAASB expects that tailoring the standard to the typical nature and circumstances of an LCE and the audit of its financial statements will be more effective and efficient. For example, auditors of LCEs will not need to spend time identifying what is applicable and what is not (e.g., as they would need to do if they were using the ISAs), as it should be clearer what the core requirements are when the nature and circumstances of the entity and the audit are less complex. The auditor would therefore be able to invest more time executing appropriate procedures that more effectively targets the risks of material misstatement, when appropriately used for an audit of an LCE.

IV. STRUCTURE AND FORMAT OF THE ISA FOR LCE

1. Format of the ISA for LCE

The ISA for LCE includes objectives, definitions, requirements and EEM.

Objectives

Because the standard is principles-based each Part of the ISA for LCE contains objective(s) to be achieved by performing procedures to comply with the requirements within that Part. The objectives focus the auditor on:

- Understanding what needs to be accomplished; and
- Deciding whether more needs to be done in the particular circumstances of the audit.

The objectives of all the Parts combined achieve the overall objectives of the auditor (see ISA for LCE, paragraph 1.3.1)

Definitions

The definitions describe the meanings attributed to certain terms for the purpose of this standard and can be found in the Glossary of Terms in Appendix 1.

The definitions assist in the consistent application and interpretation of the requirements, and are not intended to override definitions that may be established for other purposes, whether in law or regulation.

Requirements

Similar to the ISAs, the ISA for LCE sets out requirements that, taken together, would fulfill the overall objective of the auditor (i.e., to express an opinion based on the audit evidence obtained). Compliance with these requirements is intended to support how the auditor obtains sufficient appropriate audit evidence as the basis for the auditor's reasonable assurance opinion. Requirements are expressed using "shall."

The auditor is required to comply with all relevant requirements in the ISA for LCE unless it is judged to be necessary to depart (only in exceptional circumstances) to be able to achieve reasonable assurance (see ISA for LCE, paragraphs 1.4.1 and 1.4.2).

EEM

The EEM serves a similar purpose to application and other explanatory material in the ISAs, but is much more limited than what is presented within the ISAs. The EEM is targeted at a higher level (i.e., a conceptual and contextual level), taking into account the typical nature and circumstances of audits for which the standard has been designed.

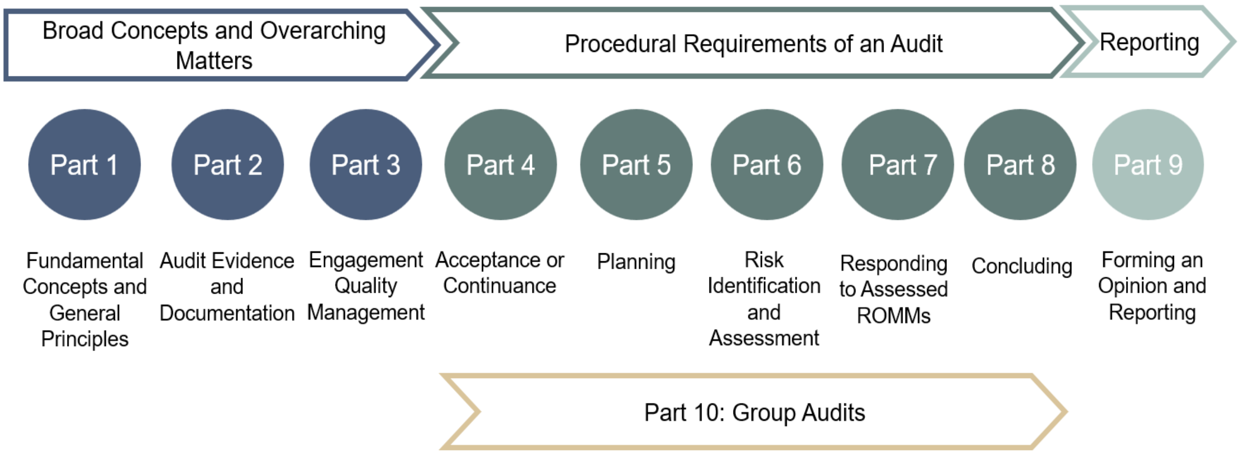
To distinguish EEM from the requirements within ISA for LCE, the EEM has been presented in italics (and highlighted in light blue). There are two types of EEM included: general introductory EEM that explains the context of the section that follows and EEM specific to the requirement directly above it. However, there is no difference in the status of each type.

EEM does not in itself impose a requirement or expand any requirement. Rather it is used when the explanation or guidance it provides is considered to be so important that including it in the standard and positioning it alongside the requirement(s) is deemed necessary and informative for a proper understanding of the requirement(s). The following sets out the broad principles used for inclusion of EEM in the ISA for LCE:

- The EEM paragraphs do not create additional obligations for the auditor and do not include a "shall."
- Not every concept or requirement is explained. EEM has only been provided when it is deemed to provide crucial support to the appropriate application of the concept or requirement(s).
- EEM is not intended to provide detailed examples about "how" to apply a requirement – rather it contains descriptions of matters relevant to understanding and applying the concepts or requirements within the ISA for LCE. For example, it may explain more precisely what the requirement means or what the requirement is intended to cover.
- If deemed necessary, the EEM may explain "why" a procedure is required to be undertaken. It may also be used to explain the iterative nature of the standard where needed.
- The EEM, where appropriate, may illustrate how a requirement could be applied for different circumstances. This illustrates scalability of the standard to the spectrum of entities that would likely fall within its remit.
- The EEM does not include background information on matters addressed in the ISA for LCE.

2. Structure of the ISA for LCE

The content (i.e., the objectives, requirements and related EEM) of the ISA for LCE have been grouped into ten Parts that follow the flow of an audit (rather than by subject matter or topic like the ISAs). The Parts are preceded by a Preface to the standard and its Authority.



Preface to the ISA for LCE	Explains the responsibilities of the auditor and management, and the design and format of the standard.
Part A, Authority of the ISA for LCE	Describes the entities for which the standard can be used. Also refer to the Authority Supplemental Guidance.
Part 1 – Part 3	Set out the broad concepts and overarching matters relevant to an audit performed using the ISA for LCE, including the overall objectives of the auditor.
Part 4 – Part 8	Set out the core requirements for an audit of an LCE following the typical flow of an audit engagement.
Part 9	Sets out requirements for forming an opinion, the content of the auditor's report, other information and comparative information. Also refer to the Auditor Reporting Supplemental Guidance.
Part 10	Sets out special considerations that apply to a group audit (i.e., additional requirements auditors must comply with when the LCE is an audit of group financial statements.)
Appendices	Appendices 1–7 contain the glossary of terms and set out certain specific considerations and matters for an audit of an LCE, as well as illustrative documents.

The same structure has been used within each Part (Parts 1–10), to help with consistency of application:

- An introductory box—setting out a summary of the content and scope of that Part. The material in the introductory boxes is not intended to create any obligations for the auditor. The IAASB considered the balance of information to include in these introductory boxes and has the view they would be helpful to quickly understand what is included in each Part.
- Objective(s)
- Requirements and EEM, including:

- Specific Communication Requirements—If there are any specific communication requirements related to the matters included in that Part, they have been grouped together so that it is clear what all the specific communications to management or those charged with governance are that need to be made.
- Specific Documentation Requirements—All the documentation requirements related to specific matters within that Part are also grouped together so that the specific matters that need to be documented are clear. An extract of all documentation requirements in the ISA for LCE are included in **Appendix 2**.

Also, considering that an engagement partner may be the only engagement team member in an audit of a LCE, the ISA for LCE includes and distinguishes requirements (and EEM) that are only applicable for engagements with more than one team member.

V. SIMILARITIES AND DIFFERENCES COMPARED TO THE ISAs

1. Key Overarching Similarities Between the ISA for LCE and the ISAs

Level of Assurance

The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements of an entity. As with an audit performed in accordance with the ISAs, the ISA for LCE contains requirements for the auditor to obtain sufficient appropriate audit evidence as a basis to express a reasonable assurance opinion. This opinion is in the form of an audit opinion communicated in the auditor's report.

Risk-Based Approach

Both the ISA for LCE and the ISAs are designed for conducting an audit engagement using a risk-based approach and use, among other, the following concepts that underpin such approach:

- Objectives for different stages of the audit engagement that together achieve the overall objectives of the auditor.
- Same core requirements and concepts as a base for establishing the work effort of the auditor when performing an audit of an LCE.
- Professional judgment and professional skepticism in planning and performing the audit engagement.
- Sufficient appropriate audit evidence as a basis for the audit opinion.
- Materiality to focus the auditor's efforts when planning and performing the audit engagement, and evaluating whether the financial statements are free from material misstatement.
- The audit risk model in identifying, assessing and responding to risks of material misstatement (i.e., the concepts of inherent risk, control risk and detection risk).

Relevant Ethical Requirements and Quality Management

Both the ISA for LCE and the ISAs require:

- The auditor to comply with relevant ethical requirements, including those pertaining to independence, for financial statement audit engagements (these ordinarily comprise the provisions of International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants* *(including International Independence Standards)* (IESBA Code) related to an audit of financial statements, together with national requirements that are more restrictive); and

- The engagement partner to be a member of a firm that applies the International Standards on Quality Management (ISQMs), or national requirements that are at least as demanding as the ISQMs.

Professional Judgment and Professional Skepticism

The underlying concepts of professional judgment and professional skepticism apply in the same way in an audit under both the ISAs and the ISA for LCE. Professional judgment and professional skepticism apply pervasively throughout an audit engagement and are reflected in various requirements in the ISAs and the ISA for LCE. For example, requirements in the ISAs to enhance the auditor’s exercise of professional skepticism around corroborative or contradictory audit evidence have been incorporated within the ISA for LCE.

2. Key Overarching Differences Between the ISA for LCE and the ISAs

Authority

- The ISA for LCE can only be used when all the criteria set out in the Authority of the standard are met.
- The ISAs can be used for audit engagements of any type, complexity or size of entity.

Structure

- The ISA for LCE is a single standard which includes ten Parts.
- The ISAs consists of thirty-seven standards.

Requirements

- The ISA for LCE does not contain requirements relating to prohibited classes of entities and do not address complex matters or circumstances.
- The ISAs contain requirements to cover a wide variety of entities with differing circumstances and sizes. The requirements in the ISAs are applicable in virtually all circumstances of audits of financial statements.

Guidance

- The ISA for LCE provides guidance in the form of EEM tailored to LCEs. Also, the guidance is located together with the related requirements.
- The ISAs provide extensive guidance in the form of application and other explanatory material. Also, the guidance is located in a designated section of each ISA, separate from the requirements.

VI. MAINTENENCE

The IAASB is committed to maintain the ISA for LCE for changes in the audit environment and is of the view that the ISA for LCE must remain up to date and, to the greatest extent possible, consistent with the ISAs. In this regard, the IAASB views the ISA for LCE as an alternative to the ISAs that has been designed to be proportionate to the typical nature and circumstances of an audit of an LCE. Therefore, the IAASB decided to update the ISA for LCE for revisions to the ISAs. To avoid having to discuss the same issues twice (e.g., when revising an ISA and when revising the ISA for LCE), the IAASB decided to start working on revising the ISA for LCE after the finalization of an ISA related project. Under this approach, the effective date of the revised ISA for LCE is likely to be one year later than the effective date of the revised or new ISA. This provides stakeholders who use the ISA for LCE with more time to prepare for the changes. When revising the ISA for LCE the IAASB will take into account the design principles of the ISA for LCE as set out in Section III.3.

Initial Period of Stability

The IAASB realizes that the adoption and implementation of the ISA for LCE will take significant time and effort from stakeholders and therefore agreed that there will be an initial period of stability of at least three years after the ISA for LCE becomes effective on December 15, 2025. This means that any potential revisions to the ISA for LCE will not become effective before December 15, 2028.

VII. TRANSITIONING

1. When to Transition from the ISA for LCE to the ISAs?

The auditor is required to consider whether the ISA for LCE is appropriate to use (in accordance with the Authority set out in Part A):

- At engagement acceptance or continuance.
- Subsequent to engagement acceptance or continuance.

At engagement acceptance or continuance, the auditor is required to consider whether the ISA for LCE is appropriate to use (see ISA for LCE, paragraph 4.3.1(b)). Part A includes requirements and guidance to help the auditor make this determination. Also, the IAASB published the Authority Supplemental Guidance which includes additional considerations that the auditor may take into account. If it is determined that there is complexity present that has not been contemplated by the ISA for LCE, the use of the ISA for LCE is not appropriate for the audit.

Subsequent to engagement acceptance or continuance, the ISA for LCE requires the auditor to re-assess the decision to use the ISA for LCE. Part 6 of the standard includes a requirement to re-assess the decision after the identification and assessment of risks of material misstatement (see ISA for LCE, paragraph 6.5.1). Also, in circumstances where audit evidence, or new information, is obtained, which is inconsistent with the auditor's original determination for using the ISA for LCE, the auditor may need to change the original determination to use the ISA for LCE, and transition to using the ISAs or other applicable auditing standards as appropriate.

It was anticipated or intended, when designing the ISA for LCE, that it should be relatively rare for an audit of an entity to need to transition after engagement acceptance or continuance from using the ISA for LCE to using the ISAs. The specific prohibitions, relevant qualitative characteristics and, if applicable, quantitative thresholds addressed in Part A will ordinarily be known at the time of engagement acceptance or continuance to inform the auditor's decision about using the ISA for LCE. Therefore, unknown complexities that would require a change for using the ISA for LCE are expected to be relatively infrequent.

To address the situation in which an entity may have initiated transactions that have resulted in complex accounting estimates in the period under audit that are not known to the auditor at the time of engagement acceptance or continuance and are discovered during the course of the audit, the standard includes the following:

- The Authority states that the entity's financial statements ordinarily do not include accounting estimates that involve the use of methods, models, assumptions, or data, that are complex. The use of the word 'ordinarily' leaves room to continue with an audit engagement under the ISA for LCE in the case there is a complex accounting estimate.
- Compared to the Exposure Draft of the ISA for LCE, more requirements and guidance related to accounting estimates have been included in Part 7 of the standard so that the auditor is able to obtain sufficient appropriate audit evidence in such circumstances.

Regardless, if there is an indicator that there may be complex matters or circumstances contrary to what the ISA for LCE has been designed to address, the auditor will need to determine whether the standard is still appropriate to use, and transition if necessary.

2. Transitioning to the ISAs Mid-Engagement

When the auditor concluded mid-engagement that the ISA for LCE can no longer be used, the auditor is required to transition to the ISAs or other applicable auditing standards.

In the case of transitioning to the ISAs, it means that the auditor is required to comply with all ISA requirements relevant to the audit to be able to represent compliance with the ISAs in the auditor's report. The incremental procedures needed will vary depending on the facts and circumstances of the audit engagement. Broadly the auditor needs to:

- Re-establish the terms of engagement, for example through the issuance of an updated engagement letter. The relevant section in the ISA for LCE is 4.4 and the relevant ISA is ISA 210.[3]

  > As per ISA for LCE, paragraph 4.7.4(a), the auditor is required to record in an audit engagement letter or other suitable form of written agreement that the audit will be undertaken using the ISA for LCE. Unless prohibited by law or regulation, it may be helpful for the auditor to make reference in the terms of the audit engagement to the possibility of transitioning to the ISAs from the ISA for LCE. In certain jurisdictions, it may be necessary for the auditor to include a reference to such possibility in order to retain the ability to do so.

- Reissue communications with management or those charged with governance. Relevant Parts in the ISA for LCE and standards in the ISAs are Part 1.8, Part 5.4, Part 6.6, Part 7.6, Part 8.8 and Part 10.7, and ISA 260 (Revised),[4] ISA 540 (Revised) and ISA 600 (Revised).[5]
- Evaluate whether sufficient work has been performed in the planning phase of the audit, including:
  - Establishing an overall audit strategy.
  - Determining whether the audit plan is sufficient and appropriate.
  - Determining whether experts or others (e.g., internal audit) need to be involved, to address the complex circumstance(s).

[3] ISA 210, *Agreeing the Terms of Audit Engagements*

[4] ISA 260 (Revised), *Communication with Those Charged with Governance*

[5] ISA 600 (Revised), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

  - Determining the work to be performed at a service organization (if applicable).

  Relevant Parts in the ISA for LCE and standards in the ISAs are Part 5.2, Part 6.3 and Part 7.4, and ISA 300,[6] ISA 402,[7] ISA 610 (Revised 2013)[8] and ISA 620.[9]

- Consider whether there are any additional procedures required on opening balances. The relevant Part in the ISA for LCE and standard in the ISAs are, Part 4.5 and ISA 510.[10]
- Evaluate the sufficiency and appropriateness of work already performed, including with respect to:
  - Understanding the entity and its environment, the applicable financial reporting framework and the entity's system of internal control, and risk identification and assessment.
  - Further audit procedures that have already been designed and performed.
  - Documentation (see ISA for LCE, Part 2.4 and ISA 230).[11]
- Design and perform additional procedures necessary to comply with all applicable ISA requirements (or requirements of other applicable auditing standards), with additional documentation as appropriate.
- Undertake other actions as considered necessary to meet the objectives of the ISAs (or requirements of other applicable auditing standards) or to meet the obligations in terms of the firm's policies or procedures.

3. Auditor Reporting

9.6.2

When the financial statements include corresponding figures or comparative financial statements and the prior period was audited under a different auditing standard (e.g., the ISAs were used for the prior period and the ISA for LCE is used for current period or vice versa), the auditor is not required to include information regarding the auditing standards used for different periods in the auditor's report. The IAASB is of the view that this is not required as both the ISAs and the ISA for LCE result in the auditor obtaining reasonable assurance as a basis for the audit opinion. Although not required, the auditor may decide to include an Other Matter paragraph to highlight that the previous period was audited using a different auditing standard.

However, the auditor is required to obtain sufficient appropriate audit evidence on the comparative information in the current year to determine if a material misstatement exists as required by ISA 710[12] and Part 9.7 of the ISA for LCE, as appropriate. For comparative financial statements, these procedures enable the auditor to obtain sufficient appropriate audit evidence to support the auditor's opinion over both periods presented.

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6 ISA 300, *Planning an Audit of Financial Statements*

7 ISA 402, *Audit Considerations Relating to an Entity Using a Service Organization*

8 ISA 610 (Revised 2013), *Using the Work of Internal Auditors*

9 ISA 620, *Using the Work of an Auditor's Expert*

10 ISA 510, *Initial Audit Engagements—Opening Balances*

11 ISA 230, *Audit Documentation*

12 ISA 710, *Comparative Information—Corresponding Figures and Comparative Financial Statements*

VIII. INSIGHTS INTO THE ISA FOR LCE

1. General

As explained earlier in this Guide, the ISA for LCE is a standalone standard which is based on the ISAs and is an alternative to the ISAs that has been designed to be proportionate to the typical nature and circumstances of an audit of an LCE. Given this, throughout the development of the standard, stakeholders asked whether it would be possible or not to refer to the ISAs for additional guidance when using the ISA for LCE to conduct an audit engagement.

The ISA for LCE does not prohibit the auditor from using knowledge obtained by reading or applying other auditing standards, including the ISAs. Auditors could potentially refer to various sources of guidance in undertaking an audit engagement.

However, when an audit engagement is undertaken using the ISA for LCE, the ISAs do not apply to the engagement. Also, the ISA requirements cannot be used to address complex matters or circumstances not contemplated in the design of the standard as this creates a risk of inappropriate use of the ISA for LCE (see Section III.1).

Example:

If the entity being audited using the ISA for LCE, started a significant new business activity in a different and emerging industry during the reporting period, this could increase complexity across the entity's business operations, information system, financial reporting process and system of internal control. If the auditor concludes that, because of the new business activity and its impact, the entity no longer meets the qualitative characteristics of an LCE, the ISA for LCE can no longer be used. The auditor would need to transition to the ISAs or other applicable auditing standard(s) to perform the audit engagement.

2. Preface to the ISA for LCE

The Preface explains the essential matters that needs to be understood when using the ISA for LCE including that:

- The standard has been designed to achieve reasonable assurance.
- The standard is premised on the basis that the firm is subject to ISQM 1[13] or to national requirements that are at least as demanding.
- The standard is written in the context of an audit of a complete set of general-purpose financial statements and may also be adapted as necessary in the circumstances of the engagement to an audit of a complete set of special purpose financial statements, or an audit of a single financial statement or of a specific element, account or item of a financial statement.
- The ISAs do not apply to the engagement when the audit engagement is undertaken using the standard.
- The standard's format.

[13] ISQM 1, *Quality Management for Firms that Perform Audits or Reviews for Financial Statements, or Other Assurance or Related Services Engagements*

- Specific considerations when applying the standard to engagements in the public sector.

Public Sector Entities

The ISA for LCE can be used for audit engagements in the public sector when the considerations set out in the Authority in Part A apply. The Preface to the ISA or LCE (paragraphs P.18–P.21) provides additional contextual information about public sector entities. As with the ISAs, the ISA for LCE includes considerations specific to public sector entities throughout the standard. These considerations are included in the EEM.

The ISA 800-Series

Requirements relating to the ISA 800-series[14] have not been included in the ISA for LCE as the IAASB agreed to focus on developing an auditing standard for audits of complete sets of general-purpose financial statements of LCEs. However, the Preface (paragraph P.2) recognizes that the ISA for LCE may be adapted as necessary in the circumstances of the engagement to an audit of a complete set of special purpose financial statements, or an audit of a single financial statement or of a specific element, account or item of a financial statement, only if the entity is an LCE as set out in Part A.

3. Part A, Authority

Part A describes the entities for which the standard can be used.

Decisions about the required or permitted use of the ISA for LCE in jurisdictions rest with legislative and regulatory authorities or relevant local bodies with standard-setting authority. At the engagement level, the engagement partner determines whether the use of the ISA for LCE is appropriate in accordance with the firms' policies or procedures and Part A (see ISA for LCE, paragraph 4.3.1). If the ISA for LCE is used for audit engagements other than those contemplated in Part A, the auditor is not permitted to represent compliance with the ISA for LCE in the auditor's report.

The Authority Supplemental Guidance provides additional information that may be of assistance when adopting and implementing the ISA for LCE. This guidance may be particularly useful to:

- Legislative or regulatory authorities or relevant local bodies with standard-setting authority (such as regulators or oversight bodies, jurisdictional / national standard setters, professional accountancy organizations or others with authority for setting auditing standards) when determining the permitted use of the ISA for LCE in an individual jurisdiction.
- Firms for developing policies or procedures in relation to the use of the ISA for LCE.
- Engagement teams or auditors when determining whether the standard is appropriate to use for a specific audit engagement at the client acceptance or continuance phase.

4. Part 1, Fundamental Concepts, General Principles and Overarching Requirements

Part 1 sets out the fundamental concepts, general principles and overarching requirements to be applied throughout the audit, including the:

- Effective date.

[14] The ISA 800-series includes: ISA 800 (Revised), *Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*; ISA 805 (Revised), *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement* and ISA 810 (Revised), *Engagements to Report on Summary Financial Statements*.

- Relevant ethical requirements and firm-level quality management.

  Relevant ethical requirements ordinarily comprise the provisions of the IESBA Code related to an audit of financial statements, together with national requirements that are more restrictive.

  The standard requires that the engagement partner is a member of a firm that applies the ISQMs, or national requirements that are at least as demanding as the ISQMs.

- Overall objectives of the auditor when conducting an audit of financial statements using the ISA for LCE.
- Overarching requirements for the auditor to exercise professional judgment and professional skepticism in planning and performing the audit.
- Overarching requirements to be applied throughout the audit with regard to the auditor's responsibilities relating to fraud, laws and regulations, and related parties. Other parts of the ISA for LCE include more specific requirements relating to these topics (e.g., risk identification and assessment in Part 6, or responding to assessed risks in Part 7).
- General requirements about communications with management and those charged with governance. Other parts of the ISA for LCE also contain relevant specific communication requirements.

5. Part 2, Audit Evidence and Documentation

Part 2 sets out general requirements for:

- Obtaining sufficient appropriate audit evidence including requirements on information to be used as audit evidence. Other parts of the ISA for LCE also include more specific requirements relating to audit evidence.
- Documentation. The guidance below elaborates on certain aspects of the documentation requirements in the ISA for LCE.

The approach to documentation in ISA for LCE is the same as the approach to documentation in the ISAs.

The documentation requirements include overarching principles in Part 2 on the basis that documentation should be sufficient to enable an experienced auditor, having no previous experience with the audit, to understand the nature, timing and extent of the audit procedures undertaken, the results of the audit procedures and the audit evidence obtained, significant matters arising during the audit and the conclusions thereon, including significant professional judgements made in reaching those conclusions.

The individual Parts contain relevant specific documentation requirements, in the same way that individual ISAs other than ISA 230 contain more specific documentation requirements, which are to be complied with in addition to the general documentation requirements set out in Part 2.

An extract of all documentation requirements in the ISA for LCE is included in **Appendix 2**.

How Proportionality is Addressed

Documentation was one of the prominent areas where the IAASB's stakeholders asked for proportionality. Therefore, guidance is included in Part 2 of the ISA for LCE to clarify how to apply the general documentation requirements in an appropriately proportional manner. Moreover, given that the requirements in the ISA for LCE are proportionate for an audit of an LCE, the corresponding documentation is expected to be more proportional as well.

Documentation of Compliance with the ISA for LCE

EEM under 2.4.1

Audit documentation provides evidence that the audit complies with the ISA for LCE. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (e.g., as in a checklist) compliance with matters for which compliance is demonstrated by documents included within the audit file.

Examples:

- The existence of a signed engagement letter in the audit file demonstrates that the auditor has agreed the terms of the audit engagement with management or, where appropriate, those charged with governance.
- An auditor's report containing an appropriately qualified opinion on the financial statements demonstrates that the auditor has complied with the requirement to express a qualified opinion under the circumstances specified in the ISA for LCE.
- In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file, such as:
    - When the audit evidence obtained includes evidence that both corroborates and contradicts management's assertions in relation to accounting estimates, documenting how the auditor evaluated that evidence, including the professional judgments made in forming a conclusion as to the sufficiency and appropriateness of the audit evidence obtained may provide evidence of the auditor's exercise of professional skepticism in accordance with the ISA for LCE.
    - Documentation on the engagement partner's participation in engagement team discussions may contribute to providing evidence that the engagement partner has taken responsibility for the direction and supervision of the engagement team.

6. Part 3, Engagement Quality Management

Part 3 sets out the engagement partner's responsibilities for managing and achieving quality for the audit engagement.

Differences of Opinion, or Difficult or Contentious Matters

EEM under 3.2.9

Differences of opinion may arise within the engagement team, or between the engagement team and the engagement quality reviewer, or even with individuals performing activities within the firm's system of quality management such as those responsible for providing consultation. Also, difficult or contentious matters may be identified during the audit that require consultations to be undertaken in accordance with the firm's related policies or procedures.

In considering matters related to differences of opinion, or difficult or contentious matters, the auditor may take further steps and identify new information or obtain additional audit evidence which is inconsistent with the auditor's original determination for using the ISA for LCE. For example, it may come to auditor's attention that the contentious matter is due to change in entity's business activities and give rise to significant pervasive business risks. This may highlight complex matters or circumstances that are not consistent with the qualitative characteristics in Part A for the use of the ISA for LCE. Therefore, in considering matters related to differences of opinion, or difficult or contentious matters, the engagement partner may also consider whether the use of the ISA for LCE continues to be appropriate.

How Proportionality is Addressed

Throughout the standard there are separate requirements for when there are members of the engagement other than the engagement partner. These are placed in a box with the header “Considerations When There Are Members of the Engagement Team Other Than the Engagement Partner” and most of these requirements are located in Part 3.

7. Part 4, Acceptance or Continuance of an Audit Engagement and Initial Audit Engagements

Part 4 sets out the auditor’s responsibilities for agreeing the terms of engagement, including establishing that the preconditions for an audit are present, and determining that the use of the ISA for LCE is appropriate. This Part also addresses requirements relating to initial audit engagements, including obtaining sufficient appropriate audit evidence about opening balances.

8. Part 5, Planning

Part 5 sets out the auditor’s responsibilities for planning the audit and applying the concept of materiality in planning and performing the audit.

Planning Activities

Planning activities include:

- Setting the scope, timing and direction of the audit;
- Undertaking an engagement team discussion;
- Fulfilling responsibilities if information to be used as audit evidence has been prepared by a management’s expert; and
- Determining whether to use the work of an auditor’s expert.

For experts, in addition to the planning matters addressed in Part 5 (paragraphs 5.2.9–5.2.12), Part 7 of the ISA for LCE sets out requirements for using the work of a management’s expert (paragraph 7.4.29) and the work of an auditor’s expert (paragraphs 7.4.30–7.4.31).

> The ISA for LCE does not distinguish between the ‘overall audit strategy’ and the ‘audit plan’ as is required by the ISAs. However, planning activities are still required to ensure that the audit will be performed in an effective manner. In the ISA for LCE, the relevant outcomes of establishing an overall audit strategy and developing an audit plan have been incorporated in the requirements to set out the scope, timing and direction of the audit (see ISA for LCE, paragraphs 5.2.1–5.2.6)

Materiality in the Context of an Audit **5.3.1**

Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements and provides a frame of reference to the auditor in determining materiality for the audit. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that:

- Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;
- Judgments about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and
- Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

The auditor's determination of materiality is a matter of professional judgment and is affected by the auditor's perception of the financial information needs of users of the financial statements. In this context, it is reasonable for the auditor to assume that users:

- Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;
- Understand that financial statements are prepared, presented and audited to levels of materiality;
- Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and
- Make reasonable economic decisions on the basis of the information in the financial statements.

Use of a Benchmark to Determine Materiality

5.3.1

The ISA for LCE, paragraph 5.3.1 requires the auditor to determine materiality for the financial statements as a whole. Although, the auditor's determination of materiality is a matter of professional judgment rather than a mechanical exercise, a percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole.

Examples:

Factors that may affect the identification of an appropriate benchmark include the following:

- **Relevant financial statement elements.** Based on the likely users of the financial statements (e.g., entity's owners and those charged with governance, financial institutions, franchisors, major funders, employees, customers, creditors, or government agencies and departments), what are the major elements of the financial statements that will be of interest to users (e.g., assets, liabilities, equity, income, and expenses)?
- **The primary focus of users.** What information in financial statement items will attract the attention of users? For example, users interested in:
    - Evaluating financial performance will focus on profits, revenues, or net assets.
    - The resources utilized to achieve certain goals or ends will focus on the nature and extent of revenues and expenditures.
- **Nature of the entity.** What is the nature of the entity, where the entity fits in the life cycle (e.g., growing, mature, declining), and the industry and economic environment in which the entity operates?

- **Financing.** How is the entity financed? If the entity is financed solely by debt rather than equity, users may put more emphasis on the pledged assets and any claims on them than on the entity's earnings.
- **Volatility.** How volatile is the proposed benchmark? If the chosen benchmark fluctuates widely, it may not be the appropriate base for determining materiality.

Determining a percentage to be applied to a chosen benchmark involves the exercise of professional judgment. There is a relationship between the percentage and the chosen benchmark, such that a percentage applied to profit before tax from continuing operations will normally be higher than a percentage applied to total revenue. For example, the auditor may consider five percent of profit before tax from continuing operations to be appropriate for a profit-oriented entity, while the auditor may consider one percent of total revenue or total expenses to be appropriate for a not-for-profit entity. Higher or lower percentages, however, may be deemed appropriate in the circumstances.

How to Determine Performance Materiality

5.3.3

The determination of performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. Performance materiality by its design is set at an amount below materiality for the financial statements as a whole, which results in more audit work, but is needed to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole (if applicable, the same applies to the materiality level(s) set for particular classes of transactions, account balances or disclosures).

Performance materiality is designed to:

- Ensure that immaterial misstatements less than materiality for the financial statements as a whole (or the materiality level(s) for particular classes of transactions, account balances or disclosures, if applicable) are detected; and
- Provide a margin or a buffer for possible undetected misstatements. This buffer is between detected but uncorrected misstatements in the aggregate, and materiality for the financial statements as a whole (or the materiality level(s) for particular classes of transactions, account balances or disclosures, if applicable).

The percentage to be applied to materiality for the financial statements as a whole (or the materiality level(s) for particular classes of transactions, account balances or disclosures, if applicable) is affected by the auditor's understanding of the entity and the nature and extent of misstatements identified in previous audits and thereby the auditor's expectations in relation to misstatements in the current period.

9. Part 6, Risk Identification and Assessment

Part 6 sets out requirements for:

- Understanding relevant aspects of the entity, including the entity and its environment, the applicable financial reporting framework and the entity's system of internal control.
- Identifying and assessing the risks of material misstatement.
- Evaluating the appropriateness of continue using the ISA for LCE.

How Proportionality is Addressed

Proportionality is addressed throughout the ISA for LCE but in particular in Part 6. Part 6 addresses proportionality considering that a LCE's system of internal control is generally straightforward and less formalized than in larger and more complex entities. As explained in the "*Key Differences Between the ISA for LCE and the Related ISAs*" section in Appendix 1, there are ISA requirements not reflected in the ISA for LCE since they were deemed not necessary, due to the typical nature and circumstances of an LCE. In Part 6, proportionality is addressed as follows:

- Understanding the entity's system of internal control
  - The work effort verb for obtaining an understanding of and evaluating the entity's risk assessment process and entity's process for monitoring the internal control system is inquiry. This is because inquiry was deemed sufficient and proportionate to a typical LCE and would appropriately drive the overall consideration of risks of material misstatements and control deficiencies as described in Part 6 (see paragraph 6.3.1(a) and (c)).
  - The detailed list of matters to be understood in ISA 315 (Revised 2019),[15] paragraph 21 about the control environment is presented as EEM under paragraph 6.3.7 in the ISA for LCE as not all matters included in ISA 315 (Revised 2019) are relevant for a typical LCE. By including these matters in the EEM, the auditor may still consider a matter but it alleviates the perceived need to provide detailed documentation in relation to all these matters.
  - The requirement related to the entity's information system and communication in ISA 315 (Revised 2019), paragraph 25 has been adapted to be more direct in the ISA for LCE and focus on the entity's process to prepare its financial statements (paragraphs 6.3.8 and 6.3.10).
- Identifying and assessing the risks of material misstatement
  - The separate requirements in ISA 315 (Revised 2019), paragraphs 28–31 relating to the identification and assessment of risks of material misstatement, and determining the relevant assertions and the related significant classes of transactions, account balances and disclosures are combined into a single requirement in paragraph 6.4.1 of the ISA for LCE, given that these matters are typically addressed in a more straightforward manner and at the same time in an audit of an LCE.

IT Environment of an LCE

6.3.8

Understanding the Entity's Process to Prepare Its Financial Statements Including the IT Environment

The information system, and related business processes, in LCEs are likely to be less sophisticated than in non-LCEs, and are likely to involve a less complex IT environment; however, the role of the information system is just as important. LCEs with direct management involvement may not need extensive descriptions of accounting procedures, sophisticated accounting records, or written policies. Understanding the relevant aspects of the entity's information system may therefore require less effort in an audit of an LCE, and may involve a greater amount of inquiry than observation or inspection of documentation. The need to obtain an understanding, however, remains important to provide a basis for the design of further audit procedures and may further assist the auditor in identifying or assessing risks of material misstatement.

[15] ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

Obtaining an understanding of the entity's IT environment may be more easily accomplished for an LCE that uses commercial software and when the entity does not have access to the source code to make any program changes. Such entities may not have dedicated IT resources but may have a person assigned in an administrator role for the purpose of granting employee access or installing vendor-provided updates to the IT applications. Specific matters that the auditor may consider in understanding the nature of a commercial accounting software package, which may be the single IT application used by an LCE in its information system, may include:

- The extent to which the software is well established and has a reputation for reliability;
- The extent to which it is possible for the entity to modify the source code of the software to include additional modules (i.e., add-ons) to the base software, or to make direct changes to data;
- The nature and extent of modifications that have been made to the software. Although an entity may not be able to modify the source code of the software, many software packages allow for configuration (e.g., setting or amending reporting parameters). These do not usually involve modifications to source code; however, the auditor may consider the extent to which the entity is able to configure the software when considering the completeness and accuracy of information produced by the software that is used as audit evidence; and
- The extent to which data related to the preparation of the financial statements can be directly accessed (i.e., direct access to the database without using the IT application) and the volume of data that is processed. The greater the volume of data, the more likely the entity may need controls that address maintaining the integrity of the data, which may include general IT controls over unauthorized access and changes to the data.

Understanding the Entity's Control Activities Including General IT Controls

6.3.12–6.3.13

The extent of the auditor's understanding of the IT processes, including the extent to which the entity has general IT controls in place, will vary with the nature and the circumstances of the entity and its IT environment, as well as based on the nature and extent of controls identified by the auditor. The number of IT applications that are subject to risks arising from the use of IT also will vary based on these factors.

Examples:

- An entity that uses commercial software and does not have access to the source code to make any program changes is unlikely to have a process for program changes, but may have a process or procedures to configure the software (e.g., the chart of accounts, reporting parameters or thresholds). In addition, the entity may have a process or procedures to manage access to the application (e.g., a designated individual with administrative access to the commercial software). In such circumstances, the entity is unlikely to have or need formalized general IT controls.
- When management is not relying on automated controls or general IT controls to process transactions or maintain the data, and the auditor has not identified any automated controls or other information processing controls (or any that depend on general IT controls), the auditor may plan to directly test any information produced by the entity involving IT and may not identify any IT applications that are subject to risks arising from the use of IT.

Example of Risks Arising from the Use of IT and Related General IT Controls

The auditor may identify some automated controls that relate to the LCE's single non-complex commercial software for financial reporting that contains standard reports generated by the software. The LCE has no ability to change the program, given lack of access to the source code. The IT infrastructure supporting the IT application relates to a single network, a single operating system, and a single database. The IT operations do not involve data backup, as manual backups are done by the finance team and there are no job-scheduling operations. As a result, the auditor identifies the processes related to access (and not to change or IT operations) as subject to risks arising from the use of IT. The auditor identifies the following risks arising from the use of IT and the general IT controls to mitigate such risks:

IT Process	Example Risks Arising from the Use of IT	Example General IT Controls
Manage Access	User-access privileges: Users have access privileges beyond those necessary to perform their assigned duties, which may create improper segregation of duties	Management approves the nature and extent of user-access privileges for new and modified user access, including standard application profiles/roles, critical financial reporting transactions, and segregation of duties
		Access for terminated or transferred users is removed or modified in a timely manner
		User access is periodically reviewed
		Privileged-level access (e.g., configuration, data and security administrators) is authorized and appropriately restricted
	System settings: Systems are not adequately configured or updated to restrict system access to properly authorized and appropriate users	Access is authenticated through unique user IDs and passwords or other methods as a mechanism for validating that users are authorized to gain access to the system. Password parameters meet company or industry standards (e.g., password minimum length and complexity, expiration, account lockout)

Controls the auditor identify may depend on system-generated reports. IT applications that produce those reports may be subject to risks arising from the use of IT. When taking a substantive approach to the audit, the auditor may decide to directly test the inputs and outputs of the report-generation process. In that case, the auditor may not identify the related IT applications as subject to risks arising from IT. Therefore, the controls over these system-generated reports may not require evaluation as part of the risk assessment process.

Significant Deficiencies in Internal Control

6.3.14

The ISA for LCE, paragraph 6.3.14 requires the auditor to determine whether one or more deficiencies have been identified in the entity's system of internal control and, if so, whether, individually or in combination, they constitute significant deficiencies. A significant deficiency in internal control is defined as a deficiency or combination of deficiencies in internal control that, in the auditor's professional judgment, is of sufficient importance to merit the attention of those charged with governance.

The significance of a deficiency or a combination of deficiencies in internal control depends not only on whether a misstatement has actually occurred, but also on the likelihood that a misstatement could occur and the potential magnitude of the misstatement.

Examples:

Indicators of significant deficiencies in internal control include:

- Evidence of ineffective aspects of the control environment, such as:
  - Indications that significant transactions in which management is financially interested are not being appropriately scrutinized by those charged with governance.
  - Identification of management fraud, whether or not material, that was not prevented by the entity's internal control.
  - Management's failure to implement appropriate remedial action on significant deficiencies previously communicated.
- Evidence of an ineffective response to identified significant risks (for example, absence of controls over such a risk).
- Misstatements detected by the auditor's procedures that were not prevented, or detected and corrected, by the entity's internal control.
- Restatement of previously issued financial statements to reflect the correction of a material misstatement due to error or fraud.
- Evidence of management's inability to oversee the preparation of the financial statements.

Inherent Risk

EEM under 6.4.1

EEM under paragraph 6.4.1 in the ISA for LCE explains that, when assessing inherent risk, factors relating to the preparation of information required by the applicable financial reporting framework that affect the susceptibility of assertions to misstatement may include complexity, subjectivity, change, uncertainty and susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk. These are further explained below:

- **Complexity**—Complexity arises either from the nature of the information or in the way that the information required by the applicable financial reporting framework (required information) is prepared, including when such preparation processes are more inherently difficult to apply.

  Example:

  Complexity may arise when there are many potential data sources, with different characteristics used in making an accounting estimate, the processing of that data involves many interrelated steps, and the data is therefore inherently more difficult to identify, capture, access, understand or process.

- **Subjectivity**—Subjectivity arises from inherent limitations in the ability to prepare required information in an objective manner, due to limitations in the availability of knowledge or information, such that management may need to make an election or subjective judgment about the appropriate approach to take and about the resulting information to include in the financial statements. Because of different approaches to preparing the required information, different outcomes could result from appropriately applying the requirements of the applicable financial reporting framework. As limitations in knowledge or data increase, the subjectivity in the judgments that could be made by reasonably knowledgeable and independent individuals, and the diversity in possible outcomes of those judgments, will also increase.

- **Change**—Change results from events or conditions that, over time, affect the entity's business or the economic, accounting, regulatory, industry or other aspects of the environment in which it operates, when the effects of those events or conditions are reflected in the required information. Such events or conditions may occur during, or between, financial reporting periods.

Example:

Change may result from developments in the requirements of the applicable financial reporting framework, or in the entity and its business model, or in the environment in which the entity operates. Such change may affect management's assumptions and judgments, including as they relate to management's selection of accounting policies or how accounting estimates are made or related disclosures are determined.

- **Uncertainty**—Uncertainty arises when the required information cannot be prepared based only on sufficiently precise and comprehensive data that is verifiable through direct observation. In these circumstances, an approach may need to be taken that applies the available knowledge to prepare the information using sufficiently precise and comprehensive observable data, to the extent available, and reasonable assumptions supported by the most appropriate available data, when it is not. Constraints on the availability of knowledge or data, which are not within the control of management (subject to cost constraints where applicable) are sources of uncertainty and their effect on the preparation of the required information cannot be eliminated.

Example:

Estimation uncertainty arises when the required monetary amount cannot be determined with precision and the outcome of the estimate is not known before the date the financial statements are finalized.

- **Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk**—Susceptibility to management bias results from conditions that create susceptibility to intentional or unintentional failure by management to maintain neutrality in preparing the information. Management bias is often associated with certain conditions that have the potential to give rise to management not maintaining neutrality in exercising judgment (indicators of potential management bias), which could lead to a material misstatement of the information that would be fraudulent if intentional. Such indicators include incentives or pressures insofar as they affect inherent risk (e.g., as a result of motivation to achieve a desired result, such as a desired profit target or capital ratio), and opportunity, not to maintain neutrality.

Fraud Risk Factors and Risks of Material Misstatement Due to Fraud

The ISA for LCE, paragraph 1.5.1(a) requires the auditor to address the risk of fraud when identifying and assessing risks of material misstatement. In doing so, the auditor is required to evaluate whether information obtained from the procedures to identify and assess risks, and related activities, indicates that one or more fraud risk factors are present.

Fraud Risk Factors

6.2.4

Fraud risk factors are events or conditions that indicate an incentive or pressure to commit fraud, or provide an opportunity to commit fraud. While fraud risk factors may not necessarily indicate the existence of fraud, they have often been present in circumstances where frauds have occurred and therefore may indicate risks of material misstatement due to fraud. Appendix 4 of the ISA for LCE sets out fraud risk factors relevant to LCEs (although these cover a broad range of situations that may be faced by auditors, they are only examples and other risk factors may exist).

The presence of fraud risk factors may affect the auditor's assessment of inherent risk or control risk.

Relationship Between Fraud Risk Factors, Inherent Risk and Control Risk

Fraud risk factors may:

- Affect inherent risk and may be due to management bias. They may also arise from complexity or uncertainty may create opportunities that result in a susceptibility to misstatement due to fraud. When fraud risk factors relate to inherent risk, the inherent risk is assessed before consideration of controls.
- Relate to events or conditions that may exist in the entity's system of internal control that provide an opportunity to commit fraud and are relevant to the consideration of the entity's controls (i.e., related to control risk), and may be an indicator that other fraud risk factors are present.

Fraud risk factors reflective of an attitude that permits rationalization of the fraudulent action may not be susceptible to observation by the auditor. Nevertheless, the auditor may become aware of the existence of such information through, for example, the required understanding of the entity's control environment.

Risks of Material Misstatement Due to Fraud

6.4.4 and 6.4.6

The ISA for LCE, paragraph 6.4.4 requires the auditor to determine whether any of the assessed risks of material misstatement are, in the auditor's professional judgment, a significant risk. In addition, as described in paragraph 6.4.6 risks of material misstatement due to fraud, including risk of material misstatement from management override of controls and risks of fraud in revenue recognition, are presumed to be significant risks.

Relevant assertions and the related classes of transactions, account balances or disclosures that may be susceptible to material misstatement due to fraud include:

- Accuracy or valuation of revenue from contracts with customers — revenue from contracts with customers may be susceptible to inappropriate estimates of the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer.
- Occurrence or classification of expenses — expenses may be susceptible to inclusion of fictitious or personal expenses to minimize tax or other statutory obligations.

- Existence of cash balances — cash balances may be susceptible to the creation of falsified or altered external confirmations or bank statements.
- Valuation of account balances involving relatively complex accounting estimates — account balances involving accounting estimates such as goodwill and other intangible assets, impairment of inventories may be susceptible to either high estimation uncertainty, significant subjectivity or management bias in making judgments about future events or conditions.
- Classification — certain income or expenses may be susceptible to misclassification within the statement of comprehensive income, for example, to manipulate key performance measures.
- Presentation of disclosures — disclosures may be susceptible to omission, or incomplete or inaccurate presentation, for example, disclosures relating to financial guarantees or debt covenant requirements.

ISA for LCE Applicability Stand-back

6.5.1

The ISA for LCE, paragraph 6.5.1 requires the engagement partner to evaluate whether the ISA for LCE continues to be appropriate for the nature and circumstances of the entity being audited, based on the procedures performed to identify and assess the risks of material misstatement. Section VII.1 discusses more broadly the auditor's responsibility to consider whether the ISA for LCE is and remains appropriate to use.

Accounting Estimates

The financial statements of an LCE ordinarily do not include accounting estimates that involve the use of methods, models, assumptions, or data that are complex (see Part A, paragraph A.3). However, accounting estimates with greater complexity may arise during the course of the audit due to unexpected events, conditions or transactions that come to auditor's knowledge and that were not known to the auditor at the time of engagement acceptance or continuance. There would be no need to "automatically" transition out of the ISA for LCE during the engagement because isolated or "one-off" accounting estimates arose. The auditor would need to consider whether the accounting estimates increase the complexity of the entity as a whole.

Example:

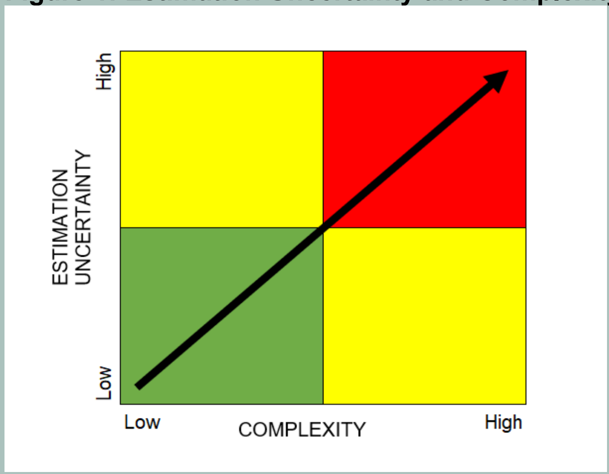
For example, an entity may enter into a single swap transaction to hedge the fluctuations of interest rates related to the debt for their building. If the other qualitative characteristics indicate that the entity is an LCE, the auditor may still determine it is appropriate to use the ISA for LCE as the swap is not typical to the entity or its transactions and is not contributing to the complexity of the entity as a whole. On the other hand, if the swap was related to their main business activities, for example, to hedge the fluctuations of currency rates related to their exports, this would likely be an indicator of complexity more pervasively that would preclude the use the standard.

Accounting Estimates

Accounting estimates vary widely in nature, and the complexity of accounting estimates are subject to, or affected by factors such as estimation uncertainty,[16] complexity[17] or subjectivity.[18]

The implications of the factors of complexity and estimation uncertainty on the complexity of accounting estimates are illustrated in Figure 1 below. For simplicity, Figure 1 only includes the factors of complexity and estimation uncertainty. The complexity is highest in the top right corner as there is a combination of high estimation uncertainty, and high complexity (e.g., such as expected credit losses, or more complex insurance contract liabilities). Conversely the lower left corner represents accounting estimates where there is a lower complexity because there is low estimation uncertainty and complexity. (e.g., such as straight-line depreciation of short-term tangible fixed assets).

Figure 1: Estimation Uncertainty and Complexity



The IAASB extensively discussed how accounting estimates may be reflected in the standard and agreed on the following key principles:

- The financial statements of LCEs ordinarily do not include accounting estimates that involve the use of methods or models, assumptions or data that are complex. Rather, the accounting estimates are often relatively straightforward and exhibit a lower degree of estimation uncertainty, complexity and subjectivity and would not fall in the 'red quadrant' in Figure 1.
- The ISA for LCE should include requirements and guidance that deal with isolated instances where more complex accounting estimates may be present. These requirements have been included in Part 7 of the ISA for LCE.

10. Part 7, Responding to Assessed Risks of Material Misstatement

Part 7 sets out requirements for:

- The design and implementation of responses to assessed risks of material misstatement at the financial statement and assertion levels, including substantive procedures and tests of controls.

16 Estimation uncertainty is the susceptibility to an inherent lack of precision in measurement. It arises when the required monetary amount for a financial statement item that is recognized or disclosed in the financial statements cannot be measured with precision through direct observation of the cost or price.

- Procedures relating to specific focus areas in an audit engagement (e.g., going concern, accounting estimates etc.).
- The auditor's responsibilities for accumulating misstatements identified during the audit.

Unpredictability as an Overall Response to Risks of Material Misstatement Due to Fraud **7.2.2**

The ISA for LCE, paragraph 7.2.2(b) requires the auditor to incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures in determining overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level. Incorporating an element of unpredictability is essential, particularly where individuals within the entity who are familiar with the audit procedures normally performed on engagements may be better positioned to conceal fraudulent financial reporting and misappropriation of assets. These individuals may become familiar or predictable with the audit procedures based on:

- Information provided to management, and where appropriate, those charged with governance with regard to planned audit procedures and their timing.
- Previous audits (e.g., what items will be selected for testing).

Examples:

In addition to examples provided in EEM under paragraph 7.2.2, incorporating an element of unpredictability may be achieved by:

- Performing tests of detail where the auditor performed substantive analytical procedures in previous audits.
- Performing substantive analytical procedures at a more detailed level or lowering thresholds when performing substantive analytical procedures for further investigation of unusual or unexpected relationships.
- Using automated tools and techniques, such as anomaly detection or statistical methods, on an entire population to identify items for further investigation.

Substantive Analytical Procedure **7.3.16**

If the auditor uses substantive analytical procedures to obtain audit evidence, the ISA for LCE, paragraph 7.3.16(e) requires the auditor to investigate fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount by:

- Inquiring of management and obtaining appropriate audit evidence relevant to management's responses; and

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[17] Complexity is the inherent complexity in the process of making an accounting estimate, before consideration of controls, which gives rise to inherent risk. Complexity may arise when:

- There are many valuation attributes with many or non-linear relationships between them.
- Determining appropriate values for one or more valuation attributes requires multiple data sets.
- More assumptions are required in making the accounting estimate, or when there are correlations between the required assumptions.
- The data used is inherently difficult to identify, capture, access or understand.

[18] Subjectivity (i.e., the subjectivity inherent in the process of making an accounting estimate, before consideration of controls) reflects inherent limitations in the knowledge or data reasonably available about valuation attributes.

- Performing additional audit procedures as necessary in the circumstances.

Obtaining appropriate audit evidence relevant to management's responses may include evaluating management's responses taking into account the auditor's understanding of the entity and its environment, and with other audit evidence obtained during the course of the audit.

The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.

Audit Sampling

7.3.17–
7.3.20

Paragraph 7.3.3 of the ISA for LCE requires the auditor, when designing tests of controls and tests of details, to determine the means of selecting items for testing that are effective in meeting the purpose of the audit procedure. Such means are selecting all items, selecting specific items and audit sampling. If the auditor determines that it is appropriate to use audit sampling, the auditor is required to apply paragraphs 7.3.17–7.3.20 as applicable to the procedure and the results of the procedure for which audit sampling is used.

In addition to the EEM in the ISA for LCE, the paragraphs below further clarify certain identified matters.

The purpose of the audit procedure (see ISA for LCE, paragraph 7.3.17(a)). The auditor's consideration of the purpose of the audit procedure, includes a clear understanding of what constitutes a deviation (in the case of tests of controls) or a misstatement (in the case of tests of details) so that all, and only those, conditions that are relevant to the purpose of the audit procedure are included in the evaluation of deviations or the projection of misstatements.

Examples:

In a test of details relating to the existence of accounts receivable, such as confirmation, payments made by the customer before the confirmation date but received shortly after that date by the client, are not considered a misstatement. Also, a misposting between customer accounts does not affect the total accounts receivable balance. Therefore, it may not be appropriate to consider this a misstatement in evaluating the sample results of this particular audit procedure, even though it may have an important effect on other areas of the audit, such as an indication of a control deficiency, the assessment of the risk of fraud or the adequacy of the allowance for doubtful accounts.

Performing audit procedures, appropriate to the purpose, on each item selected (see ISA for LCE, paragraph 7.3.17(d)). If the procedure is not applicable to the selected item, the auditor is required to perform the procedure on a replacement item. If the auditor is unable to apply the designed audit procedures, or suitable alternative procedures, to a selected item, the auditor is required to treat that item as a deviation from the prescribed control (in the case of tests of controls) or a misstatement (in the case of tests of details).

Examples:

- Necessary to test a replacement item – When a voided check is selected while testing for evidence of payment authorization, it is necessary to perform the procedure on a replacement item. If the auditor is satisfied that the check has been properly voided such that it does not constitute a deviation, an appropriately chosen replacement is examined.
- Unable to apply the designed audit procedures – When the documentation relating to a selected item has been lost, the auditor is unable to apply the designed audit procedures to a selected item.

- Perform suitable alternative procedures – When no reply has been received in response to a positive confirmation request, a suitable alternative procedure may be the examination of subsequent cash receipts together with evidence of their source and the items they are intended to settle.

Evaluating the results of the sample (see ISA for LCE, paragraph 7.3.20). In the case of tests of details, the projected misstatement plus anomalous misstatement, if any, is the auditor's best estimate of misstatement in the population. When the projected misstatement plus anomalous misstatement, if any, exceeds tolerable misstatement, the sample does not provide a reasonable basis for conclusions about the population that has been tested. The closer the projected misstatement plus anomalous misstatement is to tolerable misstatement, the more likely that the actual misstatement in the population may exceed the tolerable misstatement. Also, if the projected misstatement is greater than the auditor's expectations of misstatement used to determine the sample size, the auditor may conclude that there is an unacceptable sampling risk that the actual misstatement in the population exceeds the tolerable misstatement. Considering the results of other audit procedures helps the auditor to assess the risk that the actual misstatement in the population exceeds the tolerable misstatement, and the risk may be reduced if additional audit evidence is obtained.

Audit Procedures When Non-Compliance with Law or Regulation Is Identified or Suspected 7.4.27

The ISA for LCE, paragraph 7.4.27, sets out requirements if the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws or regulations. In particular, paragraph 7.4.27(d) requires the auditor to evaluate the implications on other aspects of the audit, including the auditor's risk assessment and the reliability of written representations and take appropriate action. Taking appropriate action will differ based on the facts and circumstances and may include obtaining legal advice. Obtaining legal advice may be appropriate if:

- Management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements.
- The auditor suspects that management or those charged with governance are involved in non-compliance, and there is no higher level of authority at the entity, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report.
- Law or regulation restrict the auditor's communication of certain matters with management and those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation.
- The auditor considers withdrawing from the engagement, where permitted by law or regulation. For example, when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances or the identified or suspected non-compliance raises questions regarding the integrity of management or those charged with governance, even when the non-compliance is not material to the financial statements.

11. Part 8, Concluding

Part 8 sets out requirements for:

- Evaluation of misstatements identified during the audit.
- Concluding activities and related evaluations, including analytical procedures, subsequent events, accounting estimates, sufficient appropriate audit evidence, going concern.
- Obtaining written representations.
- The engagement partner taking overall responsibility for managing and achieving quality on the audit engagement.

Evaluating the Effect of Uncorrected Misstatements

8.2.3

The ISA for LCE, paragraph 8.2.3 requires the auditor to determine whether uncorrected misstatements are material, individually or in aggregate. Specifically, paragraph 8.2.3(a) requires the auditor to consider the nature and size of the misstatements, and the particular circumstances of their occurrence. The nature of the misstatements and the particular circumstances of their occurrence could cause the auditor to evaluate such misstatements as material even if they are below materiality determined for the financial statements as a whole (or, if applicable, materiality determined for particular classes of transactions, account balances or disclosures).

In determining whether uncorrected misstatements by nature are material, the auditor considers uncorrected misstatements in amounts and disclosures. Such misstatements may be considered material either individually, or when taken in combination with other misstatements.

Examples:

Depending on the misstatements identified in disclosures, in determining whether uncorrected misstatements by nature are material, the auditor may consider whether:

- Identified errors are persistent or pervasive; or
- A number of identified misstatements are relevant to the same matter, and considered collectively may affect the user's understanding of that matter.

The circumstances related to some misstatements may cause the auditor to evaluate them as material, individually or when considered together with other misstatements accumulated during the audit, even if they are lower than materiality for the financial statements as a whole.

Examples:

Circumstances that may affect the evaluation include the extent to which the misstatement:

- Affects compliance with debt covenants, or other contractual requirements.
- Relates to the incorrect selection or application of an accounting policy that has an immaterial effect on the current period's financial statements but is likely to have a material effect on the future periods' financial statements.
- Masks a change in earnings or other trends, especially in the context of general economic and industry conditions.
- Affects ratios used to evaluate the entity's financial position, results of operations or cash flows.

- Has the effect of increasing management compensation (e.g., by ensuring that the requirements for the award of bonuses or other incentives are satisfied).
- Is significant having regard to the auditor's understanding of known previous communications to users of the financial statements.
- Relates to items involving particular parties (e.g., whether external parties to the transaction are related to members of the entity's management).
- Is an omission of information not specifically required by the applicable financial reporting framework but which, in the judgment of the auditor, is important to the users' understanding of the financial position, financial performance or cash flows of the entity.

If an individual misstatement is determined to be material, it is unlikely that it can be offset by other misstatements. For example, if revenue has been materially overstated, the financial statements as a whole will be materially misstated, even if the effect of the misstatement on earnings is completely offset by an equivalent overstatement of expenses. It may be appropriate to offset misstatements within the same account balance or class of transactions. However, the risk that further undetected misstatements may exist is considered before concluding that offsetting even immaterial misstatements is appropriate.

Determining whether a classification misstatement is material involves the evaluation of qualitative considerations, such as the effect of the classification misstatement on debt or other contractual covenants, the effect on individual line items or sub-totals, or the effect on key ratios. There may be circumstances where the auditor concludes that a classification misstatement is not material in the context of the financial statement as a whole, even though it may exceed the materiality level or levels applied in evaluating other misstatements. For example, a misclassification between balance sheet line items may not be considered material in the context of the financial statements as a whole when the amount of the misclassification is small in relation to the size of the related balance sheet line items and the misclassification does not affect the income statement or any key ratios.

Indication of Fraud

7.5.4

If the auditor identifies a misstatement during the audit, the ISA for LCE, paragraph 7.5.4 requires the auditor to evaluate whether the misstatement is indicative of fraud and, if there is such an indication, determine the implications on other aspects of the audit, even if the size of misstatement is not material in relation to the financial misstatements. When considering the implications of misstatements in classes of transactions, account balances and disclosures, the auditor exercises professional skepticism in accordance with paragraph 1.4.4 in the ISA for LCE.

Examples:

Depending on the circumstances, misstatements in disclosures could also be indicative of fraud, and, for example, may arise from:

- Misleading disclosures that have resulted from bias in the management's judgments.
- Extensive duplicative or uninformative disclosures that are intended to obscure a proper understanding of matters in the financial statements.

Considerations Specific to Public Sector Entities

8.2.3

In the case of an audit of a public sector entity, the evaluation whether a misstatement is material may also be affected by the auditor's responsibilities established by law, regulation or other authority to report specific matters, including, for example, fraud. Furthermore, issues such as public interest, accountability, probity and ensuring effective legislative oversight, in particular, may affect the assessment whether an item is material by virtue of its nature. This is particularly so for items that relate to compliance with law, regulation or other authority.

12. Part 9, Forming an Opinion and Reporting

Part 9 sets out the requirements for:

- Forming an opinion including the types of audit opinions.
- Content of the auditor's report.
- Comparative information and other information.

The auditor's report is the key communication to intended users of the audited financial statements. Therefore, the IAASB has the view that the auditor's report required by the ISA for LCE should provide the same information as an auditor's report under the ISAs, but with appropriate transparency for users as to which standard(s) have been used in conducting the audit engagement. These needs have been balanced with the need to keep the ISA for LCE understandable and succinct.

The IAASB incorporated the reporting requirements in a clear and concise manner, and to be consistent with the principles that have been applied for incorporating requirements from the rest of the ISAs. Part 9 of the ISA for LCE presents the reporting requirements using the following approach:

- Providing a specified content and format for an unmodified auditor's report (see Part 9.4). Departures from the wording of the report are not permitted except where required for compliance with law or regulation, or when the opinion or report needs to be modified in response to the specific engagement circumstances.
- Using tables to present requirements related to the circumstances that may lead to the modification of reports, and the text that may be used in the report where modifications occur (see Part 9.5).
- Using tables to present the form and content when using emphasis of matter, other matter, material uncertainty related to going concern and other information paragraphs (see Parts 9.6 and 9.8).
- Including requirements in a standard text format where the presentation is not specified above (across Parts 9.4–9.8, as applicable).

The IAASB is of the view that this presentation is consistent with the design of the standard, appropriate for the circumstances of an audit of an LCE, and that all requirements that would be generally relevant to an audit of an LCE have been included. In addition, the IAASB has the view that having a specified format for the auditor's report would be easier for users of the standard and improve consistency in application.

The Auditor Reporting Supplemental Guidance provides additional guidance for auditors with regard to modifications to the auditor's report when using the ISA for LCE on:

- Various elements of the auditor's report.
- Modifications to the opinion in the auditor's report.
- The use of Emphasis of Matter paragraphs within the auditor's report.
- The use of Other Matter paragraphs within the auditor's report.
- Reporting on Other Information.

- Reporting on a material uncertainty related to going concern.

13. Part 10, Audits of Group Financial Statements

Part 10 sets out special considerations that apply to an audit of group financial statements (group audit). The requirements in Part 10 are in addition to the requirements in other Parts of the ISA for LCE. All other parts of the ISA for LCE apply to a group audit (the requirements and guidance in Part 10 refer to, or expand on, the application of other parts of the ISA for LCE to a group audit).

How Proportionality is Addressed

The group audit requirements are included in a separate part rather than including requirements within the relevant parts of the ISA for LCE because this would keep the body of the standard more streamlined and easier to use, especially for audits that are not group audits.

In addition, it makes it easier for auditors of groups to see all relevant additional requirements in one place and it is easier to exclude Part 10 if a jurisdiction decided to not allow the standard to be used for group audits.

IX. ADOPTION AND IMPLEMENTATION MATERIAL AVAILABLE

In addition to this implementation guide, the materials below were published to support the adoption and implementation of the ISA for LCE:

- Basis for Conclusions;
- Fact sheet;
- Auditor Reporting Supplemental Guidance;
- Authority Supplemental Guidance;
- Adoption Guide;
- Frequently Asked Questions;
- Overview Presentation Deck;
- Video Series “Navigating the ISA for LCE” which includes three videos that explain:
  - The objectives, benefits and distinguishing features compared to the full suite of ISAs
  - The conditions under which the standard can be applied, including the role of legislative and regulatory authorities
  - The standard’s design principles, structure and content layout.
- Webinar that explains the standard's purpose, authority, structure and associated benefits.

All materials are published on the IAASB website: iaasb.org/ISAforLCE

Appendix 1

Comparison to ISAs

Similar to the ISAs, the ISA for LCE sets out requirements that, taken together, provide the standards for the auditor's work in fulfilling the overall objectives of the auditor. Compliance with these requirements is intended to support the auditor obtaining sufficient appropriate audit evidence as a basis for the auditor's conclusions and reasonable assurance opinion.

The IAASB has used the core requirements of the ISAs as the basis for the requirements of the ISA for LCE, but adapted the requirements to be proportionate to the typical nature and circumstances of an audit of an LCEs. See Section III.3 and Sections V.1 and 2 of the Guide that discuss the design principles of the ISA for LCE and the key overarching similarities and differences with the ISAs, respectively.

Although the ISA for LCE is based on the core requirements of the ISAs, it does not include any requirements addressing:

1. Procedures or matters typically relevant to listed entities, including reporting on segment information (ISA 501)[19] or key audit matters (ISA 701).[20]
2. When the auditor intends to use the work of internal auditors (ISA 610 (Revised 2013)), as this would ordinarily not be applicable to an audit of an LCE.
3. When the auditor intends to use a report provided by a service auditor of a service organization (ISA 402) either as audit evidence about the design and implementation of controls at the service organization (i.e., a type 1 or type 2 report), or as audit evidence that controls at the service organization are operating effectively (i.e., a type 2 report), as this would ordinarily not be applicable to an audit of an LCE.

In addition to differences caused by the three matters noted in the previous paragraph, when comparing the requirements in the ISAs and the ISA for LCE, differences can be grouped into the following categories:

1. Requirements in the ISA for LCE which have no equivalent in the ISAs.
2. Requirements in the ISAs which have no equivalent in the ISA for LCE.
3. Equivalent requirements in the ISAs and in the ISA for LCE that have the same intent, although their wording or construct are different.
4. Requirements in the ISA for LCE which combine multiple requirements in the ISAs.
5. Requirements presented in multiple paragraphs in the ISA for LCE (and in different Parts, as appropriate) which are a single paragraph in the ISAs.

For each part, the key differences resulting from **categories 1 and 2** are explained below.

The differences in **category 3** are mostly because the requirements in the ISA for LCE needed to be adapted to the typical nature and circumstances of an audit of an LCE. These differences are not expected to change the auditor's actions and outcome if applied under the same circumstance.

[19] ISA 501, *Audit Evidence—Specific Considerations for Selected Items*

[20] ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

Example:

The ISA for LCE, paragraph 8.4.2 is based on ISA 560,[21] paragraph 7(d). The reference to "latest subsequent interim financial statements" in paragraph 7(d) has been changed to a more general "monthly or quarterly financial information" in paragraph 8.4.2 since it is unlikely that an LCE will issue interim financial statements.

The differences in category 4 are mostly to improve the readability and understandability in the ISA for LCE by combining similar requirements in the ISAs. These differences are not expected to change the auditor's actions and outcome if applied under the same circumstance.

Example:

For example, the ISA for LCE, paragraph 1.6.2 is based on ISA 240,[22] paragraph 44 and ISA 250 (Revised),[23] paragraph 29.

The differences in **category 5** are mostly because of changes to improve the readability and understandability in the ISA for LCE or to reflect the structure and format of the ISA for LCE (e.g., the flow of the Parts). These differences are not expected to change the auditor's actions and outcome if applied under the same circumstance.

Examples:

- ISA 260 (Revised), paragraph 15 is addressed in the ISA for LCE, paragraphs 5.4.1 and 6.6.1 to align with the structure of the standard (i.e., Part 5, planning and Part 6, risk identification and assessment).
- ISA 220 (Revised),[24] paragraph 14 is addressed in the ISA for LCE, paragraphs 3.2.1 and 3.2.3. Paragraph 3.2.3 is a requirement located in a box of "Considerations When There Are Members of the Engagement Team Other Than the Engagement Partner".

[21] ISA 560, *Subsequent Events*

[22] ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

[23] ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

[24] ISA 220 (Revised), *Quality Management for An Audit of Financial Statements*

1. Part 1, Fundamental Concepts, General Principles and Overarching Requirements

Related ISAs[25] [26]

Part 1 is mostly based on the following ISAs:

- ISA 200[27] which deals with the independent auditor's overall responsibilities when conducting an audit of financial statements in accordance with ISAs.
- ISA 240 which deals with the auditor's responsibilities relating to fraud in an audit of financial statements.
- ISA 250 (Revised) which deals with the auditor's responsibility to consider laws and regulations in an audit of financial statements.
- ISA 260 (Revised) which deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements.

Key Differences Between the ISA for LCE and the Related ISAs

- The ISA for LCE, paragraph 1.8.4 has no equivalent requirement in the ISAs. This paragraph requires the auditor to use professional judgment in determining the appropriate form, timing, and general content of the communications with management, and where appropriate, those charged with governance. It was added to provide more clarity to the auditor's responsibilities under the ISA for LCE.
- ISA 260 (Revised), paragraphs 12 and 19 are not reflected in the ISA for LCE since these requirements relate to more complex entities (e.g., with a more complex organizational structure).

2. Part 2, Audit Evidence and Documentation

Related ISAs

Part 2 is mostly based on the following ISAs:

- ISA 230 which deals with the auditor's responsibility to prepare audit documentation for an audit of financial statements.
- ISA 260 (Revised) which deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements.
- ISA 500[28] which deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.

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25 The related ISAs noted in this appendix are based on the effective standards as of December 15, 2024.

26 This section for each part only references the ISAs on which that part is mainly based. Therefore, the ISAs noted in relation to each part is not intended to be a complete list.

27 ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

28 ISA 500, *Audit Evidence*

Key Difference Between the ISA for LCE and the Related ISAs

- ISA 230, paragraph 13 is not reflected in the ISA for LCE since this ISA requirement is a conditional requirement in exceptional circumstances. Requirements resulting from exceptional circumstances are generally not included in the ISA for LCE.

3. Part 3, Engagement Quality Management

Related ISAs

Part 3 is mostly based on ISA 220 (Revised) which deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner.

Key Differences Between the ISA for LCE and the Related ISAs

There are no key differences between the ISA for LCE and the related ISAs identified.

In making Part 3 more proportionate to the typical nature and circumstances of an audit of an LCE, the IAASB made several changes to the ISA requirements Part 3 is based on. These changes are relatively more significant than the changes made to other parts. However, because many of these changes fall into categories 3 and 4 as explained above, these changes are not explained in this appendix. The Part looks and flows differently compared to ISA 220 (Revised) but still results in appropriate outcomes relating to managing and achieving quality at the engagement level. Also see "*How Proportionality is Addressed"* in Section VIII.6.

4. Part 4, Acceptance or Continuance of an Audit Engagement and Initial Audit Engagements

Related ISAs

Part 4 is mostly based on the following ISAs:

- ISA 210 which deals with the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance.
- ISA 510 which deals with the auditor's responsibilities relating to opening balances in an initial audit engagement.

Key Differences Between the ISA for LCE and the Related ISAs

- The ISA for LCE, paragraphs 4.3.1(b), 4.7.2 and 4.7.3 have no equivalent requirements in the ISAs. These requirements are specific to the ISA for LCE as they relate to the determination whether the use of the ISA for LCE is appropriate.
- ISA 210, paragraphs 18 to 20 are not reflected in the ISA for LCE since it is not expected that the conditions (i.e., there are conflicts between financial reporting standards and additional requirements supplemented by law or regulation, or the auditor has determined that the financial reporting framework prescribed by law or regulation would be unacceptable) will be a common occurrence for LCEs. If there are local laws or regulations that conflict with financial reporting frameworks, then local bodies would identify this when adopting the ISA for LCE and decide how to resolve the conflict.

5. Part 5, Planning

Related ISAs

Part 5 is mostly based on the following ISAs.

- ISA 240 which deals with the auditor's responsibilities relating to fraud in an audit of financial statements.
- ISA 300 which deals with the auditor's responsibility to plan an audit of financial statements.
- ISA 315 (Revised 2019) which deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.
- ISA 320[29] which deals with the auditor's responsibility to apply the concept of materiality in planning and performing an audit of financial statements.
- ISA 620 which deals with the auditor's responsibilities relating to the work of an individual or organization in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence (i.e., auditor's experts).

Key Differences Between the ISA for LCE and the Related ISAs

There are no key differences between the ISA for LCE and the related ISAs identified.

6. Part 6, Risk Identification and Assessment

Related ISAs

Part 6 is mostly based on the following ISAs.

- ISA 240 which deals with the auditor's responsibilities relating to fraud in an audit of financial statements.
- ISA 315 (Revised 2019) which deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.
- ISA 402 which deals with the user auditor's responsibility to obtain sufficient appropriate audit evidence when a user entity uses the services of one or more service organizations.
- ISA 540 (Revised) which deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements.
- ISA 550[30] which deals with the auditor's responsibilities relating to related party relationships and transactions in an audit of financial statements.

Key Differences Between the ISA for LCE and the Related ISAs

In making Part 6 more proportionate to the typical nature and circumstances of an audit of an LCE, the IAASB made several changes to the ISA requirements that Part 6 is based on. These changes are relatively more significant than the changes made to other parts. However, because many of these changes fall into categories 3 and 4 as explained above, these changes are not explained in this

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29 ISA 320, *Materiality in Planning and Performing an Audit*

30 ISA 550, *Related Parties*

appendix. The Part looks and flows differently compared to the related ISAs but still results in appropriate outcomes relating to obtaining an understanding and identifying and assessing the risks of material misstatements as a basis to design and perform audit procedures responsive to assessed risks.

Also see "*How Proportionality is Addressed*" in Section VIII.9. This section states that a LCE's system of internal control is generally straightforward and less formalized than in larger and more complex entities and therefore there are ISA requirements not reflected in the ISA for LCE since they were deemed not necessary, due to the typical nature and circumstances of an LCE.

- Paragraphs 6.5.1 and 6.7.2 have no equivalent requirements in the ISAs. They are specific requirements in the ISA for LCE which requires the auditor to:
    - Evaluate the appropriate use of the ISA for LCE once risk identification and assessment has been done and the auditor has a more thorough understanding of the entity; and
    - Document the auditor's evaluation of the appropriate use of the ISA for LCE.
- ISA 315 (Revised 2019), paragraph 23 is not reflected in the ISA for LCE. This is a conditional requirement that applies when the auditor identifies risks of material misstatement that management failed to identify. A typical LCE is less likely to have formal processes around risk assessment and the process is likely to be straightforward. This is also reflected in the fact that the work effort verb for obtaining an understanding of the entity's risk assessment process is "inquiry." Inquiry was deemed sufficient and proportionate to an audit of an LCE (see ISA for LCE, paragraph 6.3.1(a)).
- ISA 315 (Revised 2019), paragraph 36 is not reflected in the ISA for LCE. This paragraph requires the auditor to evaluate whether the auditor's determination on significant classes of transactions, account balances or disclosures remains appropriate. The nature of classes of transactions, account balances and disclosures in an LCE are expected to be simpler and not made up from numerous disaggregated sources, therefore the determination of significant classes of transactions, account balances and disclosures in an audit of an LCE risk assessment is likely to be straightforward. Also see "*How Proportionality is Addressed*" in Section VIII.9 that addresses how several requirements in ISA 315 (Revised 2019) relating to the identification and assessment of risks of material misstatement, and determining the relevant assertions and the related significant classes of transactions, account balances and disclosures are combined into a single requirement in paragraph 6.4.1 of the ISA for LCE.

7. Part 7, Responding to Assessed Risks of Material Misstatement

Related ISAs

Part 7 is mostly based on the following ISAs:

- ISA 240 which deals with the auditor's responsibilities relating to fraud in an audit of financial statements.
- ISA 250 (Revised) which deals with the auditor's responsibility to consider laws and regulations in an audit of financial statements.

- ISA 330[31] which deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with ISA 315 (Revised 2019) in an audit of financial statements.
- ISA 450[32] which deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.
- ISA 501 which deals with specific considerations by the auditor in obtaining sufficient appropriate audit evidence in accordance with ISA 330, ISA 500 and other relevant ISAs, with respect to certain aspects of inventory, litigation and claims involving the entity, and segment information in an audit of financial statements.
- ISA 505[33] which deals with the auditor's use of external confirmation procedures to obtain audit evidence in accordance with the requirements of ISA 330 and ISA 500.
- ISA 530[34] which deals with the auditor's use of statistical and non-statistical sampling when designing and selecting the audit sample, performing tests of controls and tests of details, and evaluating the results from the sample.
- ISA 540 (Revised) which deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements.
- ISA 550 which deals with the auditor's responsibilities relating to related party relationships and transactions in an audit of financial statements.
- ISA 570 (Revised)[35] which deals with the auditor's responsibilities in an audit of financial statements relating to going concern and the implications for the auditor's report.

Key Differences Between the ISA for LCE and the Related ISAs

- ISA 250 (Revised), paragraph 25 is not reflected in the ISA for LCE. This paragraph requires the auditor to communicate with the next higher level of authority above management or those charged with governance. In the case of an LCE, it is expected to be unlikely that there is a higher level of authority beyond those charged with governance. Where a higher level of authority does exist, it is likely to be clear who to communicate with where non-compliance does exist. Also, where this is common in a local jurisdiction, local bodies would identify this as part of their consideration for use of the ISA for LCE and when adding any local additional requirements or guidance.
- ISA 330, paragraph 23 is not reflected in the ISA for LCE. This is a conditional requirement that requires the auditor to evaluate whether the related assessment of risk and the planned nature, timing or extent of substantive procedures covering the remaining period need to be modified, if misstatements that the auditor did not expect when assessing the risks of material misstatement are detected at an interim date. In the ISA for LCE, less focus has been placed on the performance of interim procedures since the audit of an LCE is likely to occur after year end. General requirements about interim testing have been included at 7.3.15. Also, paragraph 6.4.9 requires the auditor to

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31 ISA 330, *The Auditor's Responses to Assessed Risks*

32 ISA 450, *Evaluation of Misstatements Identified during the Audit*

33 ISA 505, *External Confirmations*

34 ISA 530, *Audit Sampling*

35 ISA 570 (Revised), *Going Concern*

revise the assessment of the risks of material misstatement and modify the further planned audit procedures in circumstances where the auditor obtains audit evidence from performing further audit procedures, or if new information is obtained, either of which is inconsistent with the audit evidence on which the auditor originally based the assessment.

- ISA 540 (Revised), paragraphs 23(d) and 25(d) are not reflected in the ISA for LCE since financial statements of LCEs ordinarily do not include accounting estimates that involve the use of methods or models, assumptions or data thar are complex. Rather, the accounting estimates are often relatively straightforward and exhibit a lower degree of estimation uncertainty, complexity and subjectivity. The following paragraphs were therefore not included:
  - Paragraph 23(d) is a conditional requirement when management's application of the method involves complex modeling.
  - Paragraph 25(d) requires the auditor's further audit procedure to address whether the data has been appropriately understood or interpreted by management. This requirement is related to more complex circumstances such as when there are complex legal or contractual terms.
- ISA 505, paragraph 15 is not reflected in the ISA for LCE. This paragraph relates to negative confirmations, and it has been excluded from the ISA for LCE because, as explained in ISA 505, negative confirmations provide less persuasive audit evidence and cannot be used as the sole substantive procedure to address an assessed risk of material misstatement, other than in very specific circumstances. Also, negative confirmations are rarely used.

8. Part 8, Concluding

Related ISAs

Part 8 is mostly based on the following ISAs:

- ISA 330 which deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with ISA 315 (Revised 2019) in an audit of financial statements.
- ISA 450 which deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.
- ISA 540 (Revised) which deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements.
- ISA 560 which deals with the auditor's responsibilities relating to subsequent events in an audit of financial statements.
- ISA 570 (Revised) which deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.
- ISA 580 [36] which deals with the auditor's responsibility to obtain written representations from management and, where appropriate, those charged with governance in an audit of financial statements.

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[36] ISA 580, *Written Representations*

Key Difference Between the ISA for LCE and the Related ISAs

- ISA 560, paragraph 12 is not reflected in the ISA for LCE. This is a conditional requirement that is applicable where law, regulation or the financial reporting framework does not prohibit management from restricting the amendment of the financial statements to the effects of the subsequent event or events causing that amendment, and those responsible for approving the financial statements are not prohibited from restricting their approval to that amendment. It is not expected that this would be a common occurrence for an audit of an LCE and therefore not included.

9. Part 9, Forming an Opinion and Reporting

Related ISAs

Part 9 is mostly based on the following ISAs:

- ISA 570 (Revised) which deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.
- ISA 700 (Revised)[37] which deals with the auditor's responsibility to form an opinion on the financial statements.
- ISA 705 (Revised)[38] which deals with the auditor's responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with ISA 700 (Revised), the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary.
- ISA 706 (Revised)[39] which deals with Emphasis of Matter paragraphs and Other Matter paragraphs in the auditor's report.
- ISA 710 which deals with the auditor's responsibilities relating to comparative information in an audit of financial statements.
- ISA 720 (Revised)[40] which deals with the auditor's responsibilities relating to other information, whether financial or non-financial information (other than financial statements and the auditor's report thereon), included in an entity's annual report.

Key Differences Between the ISA for LCE and the Related ISAs

- ISA 700 (Revised), paragraphs 43, 44 and 45 are conditional requirements when the auditor addresses other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibilities under the ISAs. These requirements are not specifically included in the body of the specified format and content of the Auditor Report in Part 9.4 of the ISA for LCE. However, paragraph 9.4.1(c) references other reporting responsibilities as an exception to depart from the specified format and content. Illustrative wordings on Other Reporting Responsibilities are addressed in the Auditor Reporting Supplemental Guidance, including within an illustrative example report.

[37] ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

[38] ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

[39] ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

[40] ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

- ISA 700 (Revised), paragraphs 53 and 54 relate to supplementary information. These paragraphs are conditional and apply if there is supplementary information that is not required by the applicable financial reporting framework that is presented with the audited financial statements. Supplementary information was deemed to be less common for financial statements of LCEs. Also, where this is common in a jurisdiction, local bodies would identify this as part of their consideration for use of the ISA for LCE and when adding any local additional requirements or guidance.
- ISA 705 (Revised), paragraph 10 deals with a disclaimer of an opinion and is not reflected in the ISA for LCE since this ISA requirement is a conditional requirement and only applies in extremely rare circumstances. Requirements resulting from exceptional circumstances are generally not included in the ISA for LCE.
- ISA 705 (Revised), paragraphs 12 and 13 are conditional requirements relating to an inability to obtain sufficient appropriate evidence due to a management-imposed limitation. These paragraphs are not reflected in the ISA for LCE because of the approach taken to forming an opinion and reporting (as discussed in Section VIII.12) is different for the ISA for LCE. The basic principles and outcomes relating to concluding whether sufficient appropriate audit evidence has been obtained, obtaining additional audit evidence when needed and appropriately modifying the auditor's opinion or withdrawing from the engagement are addressed in paragraphs 1.3.4, 8.5.5, 8.5.6, 9.5.1 and 9.5.2. Also, the gravity of situations contemplated in these ISA requirements are likely less common in audits of LCEs.
- ISA 705 (Revised), paragraph 15 is not reflected in the ISA for LCE. This paragraph relates to a situation where the auditor also expresses an opinion on a single financial statement or one or more specific elements, accounts or items of a financial statement and the ISA for LCE does not address such situations directly (also see Section VIII.2).
- ISA 720 (Revised), paragraph 19, is a conditional requirement in case the auditor concludes that a material misstatement exists in other information obtained after the date of the auditor's report. This requirement has not been reflected in the ISA for LCE because of the expected nature of other information for LCEs.
- ISA 720 (Revised), paragraph 24 is a conditional requirement in case the auditor is required by law or regulation of a specific jurisdiction to refer to the other information in the auditor's report using a specific layout or wording. This requirement is not reflected in the ISA for LCE as, based on the expected profile of what constitutes an LCE, it is not expected that this will be a common occurrence. Paragraph 9.4.1 sets out the specified format and content of the auditor's report in an audit of an LCE and the circumstances under which there can be departures. If local laws or regulations require something different in relation to the other information section in the auditor's report, then local bodies would identify this when adopting the ISA for LCE and decide how to address the situation.

10. Part 10, Audits of Group Financial Statements

Related ISAs

Part 10 is based on ISA 600 (Revised) which deals with special considerations that apply to a group audit, including in those circumstances when component auditors are involved.

Key Differences Between the ISA for LCE and the Related ISAs

- ISA 600 (Revised), paragraphs 23, 24, 25, 26, 27, 28, 29, 31, 32, 34, 36, 41, 42, 43, 44, 45, 46, 47, 48, 50, 53 and 56 are not included as these paragraphs are applicable when component auditors are involved in the group audit. The Authority of the ISA for LCE prohibits the use of the standard when component auditors are involved, except when the component auditor's involvement is limited to circumstances in which a physical presence is needed for a specific audit procedure for the group audit. In these circumstances, it is expected that the coordination with the component auditor would be straightforward and that these requirements in ISA 600 (Revised) would not be needed.
- ISA 600 (Revised), paragraphs 20, 21, 39 and 40 are not included in the ISA for LCE, as they relate to complex matters that are not contemplated as part of the qualitative characteristics for group audits in paragraph A.3 of the ISA for LCE:
    - ISA 600 (Revised), paragraphs 20 and 21 relates to restrictions on access to information or people; and
    - Different accounting policies or reporting dates in a component (ISA 600 (Revised), paragraphs 39 and 40).

In addition to the paragraphs noted above, other paragraphs in ISA 600 (Revised) were also not included as these were deemed to be addressed in the context of an LCE in the other parts of the ISA for LCE. These changes fall into categories 3 and 4 as explained above and are therefore not explained in this appendix.

Appendix 2

Documentation Requirements

The ISA for LCE contains "General Documentation Requirements" in Part 2.4 and "Specific Documentation Requirements" in each relevant Part. The general documentation requirements apply throughout the audit engagement. The "Specific Documentation Requirements" are to clarify how the documentation requirements in Part 2.4 apply in the circumstances of those Parts (i.e., for certain stages or specific aspects of the audit engagement), and to support consistent application of Part 2.4.

Below are extracts of all documentation requirements in the ISA for LCE in Parts 1 to 10. A documentation requirement applies only to requirements that are relevant in the circumstances.

1. Fundamental Concepts, General Principles and Overarching Requirements

1.9. Specific Documentation Requirements

1.9.1. The auditor shall include in the audit documentation communications about fraud made to management, those charged with governance, regulators and others.

2. Audit Evidence and Documentation

2.4. General Documentation Requirements

2.4.1. The auditor shall prepare audit documentation on a timely basis that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

(a) The nature, timing and extent of the audit procedures performed in accordance with this standard and applicable legal and regulatory requirements, including recording:

(i) The identifying characteristics of the specific items or matters tested;

(ii) Who performed the work and the date such work was completed;

(iii) Who reviewed the audit work performed and the date and extent of such review.

(b) The results of the audit procedures performed, and the audit evidence obtained; and

(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

2.4.2. If the auditor identified information that is inconsistent with the auditor's conclusion regarding a significant matter, the auditor shall document how the inconsistency was addressed by the auditor.

2.4.3. If, in exceptional circumstances, the auditor judges it necessary to depart from a relevant requirement of this standard, the auditor shall document how the alternative audit procedures performed achieve the aim of that requirement, and the reasons for the departure.

2.4.4. The auditor shall document discussions of significant matters with management, and where appropriate, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place.

Documentation of Communications

2.4.5. Where matters required to be communicated by this standard are communicated orally, the auditor shall include them in the audit documentation, and when and to whom they were communicated.

2.4.6. Where matters have been communicated in writing, the auditor shall retain a copy of the communication as part of the audit documentation. Written communications need not include all matters that arose during the audit.

3. Engagement Quality Management

3.3. Specific Documentation Requirements

3.3.1. The auditor shall include in the audit documentation:

(a) Matters identified, relevant discussions, and conclusions reached with respect to fulfillment of responsibilities for relevant ethical requirements, including applicable independence requirements.

(b) If the audit engagement is subject to an engagement quality review, that the engagement quality review has been completed on or before the date of the auditor's report.

4. Acceptance or Continuance of an Audit Engagement and Initial Audit Engagements

4.7. Specific Documentation Requirements

4.7.1. The auditor shall include in the audit documentation matters identified, relevant discussions with personnel, and conclusions reached with respect to the acceptance and continuance of the client relationship and audit engagement.

4.7.2. The auditor shall document the basis for the determination made for using the ISA for LCE.

4.7.3. The auditor shall document changes, if any, to the determination of the use of the ISA for LCE if further information comes to the auditor's attention during the audit that may change the professional judgment made in this regard.

4.7.4. The auditor shall record in an audit engagement letter or other suitable form of written agreement:

(a) That the audit will be undertaken using the ISA for LCE;

(b) The objective and scope of the audit of the financial statements;

(c) The respective responsibilities of the auditor and management;

(d) Identification of the applicable financial reporting framework for the preparation of the financial statements;

(e) Reference to the expected form and content of any reports to be issued by the auditor; and

(f) A statement that there may be circumstances in which a report may differ from its expected form and content.

4.7.5. If law or regulation prescribes in sufficient detail the terms of the audit engagement referred to in this standard, the auditor need not record them in a written agreement, except for the fact that such law or regulation applies, and that management acknowledges and understands its responsibilities.

5. Planning

5.5. Specific Documentation Requirements

5.5.1. The auditor shall include in the audit documentation a description of the scope, timing and direction of the audit, including the nature, timing and extent of procedures to be performed, and significant changes made during the audit, together with the reasons for such changes.

Considerations When There Are Members of the Engagement Team Other Than the Engagement Partner

5.5.2. The auditor shall include in the audit documentation the matters discussed among the engagement team and significant decisions reached, including the significant decisions regarding the susceptibility of the entity's financial statements to material misstatement due to fraud.

5.5.3. The auditor shall include in the audit documentation the:

(a) Following amounts and the factors considered in their determination (including any revisions as applicable):

(i) Materiality for the financial statements as a whole;

(ii) If applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures; and

(iii) Performance materiality.

(b) Amount below which misstatements would be considered clearly trivial.

6. Risk Identification and Assessment

6.7. Specific Documentation Requirements

6.7.1. The auditor shall include the following in the audit documentation:

(a) Key elements of the understanding obtained regarding each of the aspects of the entity and its environment, the applicable financial reporting framework, the entity's system of internal control, and the procedures performed to identify and assess risks of material misstatement;

(b) The names of the identified related parties (including changes from prior period) and the nature of the related party relationships;

(c) The identified and assessed risks of material misstatement, including risks due to fraud, at the financial statement level and at the assertion level, including significant risks and risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence, and the rationale for the significant judgments made;

(d) If applicable, the reasons for the conclusion that there is not a risk of material misstatement due to fraud related to revenue recognition;

(e) The controls set out in paragraphs 6.3.12 and 6.3.13 and the evaluation whether the control is designed effectively and determination whether the control has been implemented; and

(f) For accounting estimates, key elements of the auditor's understanding of the accounting estimates, including controls as appropriate, the linkage of the assessed risks of material misstatements to the auditor's further procedures, and any indicators of management bias and how those were addressed.

6.7.2. The auditor shall document the basis for the evaluation about whether the ISA for LCE continues to be appropriate for the nature and circumstances of the entity being audited.

7. Responding to Assessed Risks of Material Misstatement

7.7. Specific Documentation Requirements

7.7.1. The auditor shall include the following in the audit documentation:

(a) The overall responses to the assessed risks of material misstatement at the financial statement level;

(b) The linkage between the procedures performed and the assessed risks at the assertion level;

(c) The results of the audit procedures, including the conclusions where these are not otherwise clear;

(d) The results of audit procedures designed to address the risk of management override of controls;

(e) All misstatements accumulated during the audit and whether they have been corrected; and

(f) If the auditor plans to use audit evidence about the operating effectiveness of controls obtained in previous audits, the conclusions reached about relying on such controls that were tested in a previous audit.

7.7.2. Where the assessed risk of material misstatement is due to fraud, the auditor's documentation shall include the specific fraud response.

7.7.3. Where the auditor has identified or suspected non-compliance with laws and regulations, the auditor shall document:

(a) The results of discussion with management, and where appropriate, those charged with governance and others; including how the matter has been responded to; and

(b) The audit procedures performed, the significant professional judgments made, and the conclusions reached thereon.

7.7.4. In respect of accounting estimates, the auditor shall document significant judgments relating to the auditor's determination of whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated.

8. Concluding

8.9. Specific Documentation Requirements

8.9.1. The auditor shall include the following in the audit documentation:

(a) All misstatements accumulated during the audit and whether they have been corrected, and the auditor's conclusion as to whether the uncorrected misstatements are material, individually or in aggregate, and the basis for that conclusion; and

(b) The nature and scope of, and conclusions from, consultations undertaken during the audit, including how such conclusions were implemented.

8.9.2. The auditor's documentation shall demonstrate that information in the financial statements agrees or reconciles with the underlying accounting records, including agreeing or reconciling disclosures, whether such information is obtained from within or outside of the general and subsidiary ledgers.

8.9.3. The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report.

8.9.4. After assembly of the final audit file is complete, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period.

8.9.5. If applicable, the auditor shall document the failure to meet an objective of any Part of the ISA for LCE, and the resulting action (such as the effect on the auditor's opinion or withdrawal from the engagement if the overall objective of the auditor cannot be met).

8.9.6. If the auditor finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, the auditor shall, regardless of the nature of the modifications or additions, document:

(a) The specific reasons for making them; and

(b) When and by whom they were made and reviewed.

9. Forming an Opinion and Reporting

9.9. Specific Documentation Requirements

9.9.1. The auditor shall document the procedures performed in relation to other information and the final version of the other information.

10. Audits of Group Financial Statements

10.8. Specific Documentation Requirements

10.8.1. The auditor shall include in the audit documentation:

(a) The basis for the auditor's determination of components for purposes of planning and performing the group audit;

(b) The basis for the determination of component performance materiality; and

(c) Key elements of the understanding of the group's system of internal control.

This document was prepared by the Staff of the International Auditing and Assurance Standards Board (IAASB).

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