



NZAuASB Board Meeting Agenda

Wednesday, 7 August 2024

9:00 am to 5.00 pm, XRB Offices, Level 6, 154 Featherston Street (Wellington Chambers).

Apologies: None

Est.Time	Item	Topic	Objective		Page	Supplementary
B: PUBLIC SESSION						
10am	2	<u>Board Management</u>				
	2.1	Action list	Approve	Paper		
	2.2	Chair's report	Note	Verbal		
	2.3	AUASB Update	Note	Verbal		
	2.4	Update from CE	Note	Verbal		
10:15am	3	<u>NZAuASB workplan</u>				
	3.1	2024/25 Prioritisation schedule	Consider	Paper	3	
	3.2	IAASB meeting report	Note	Paper		3
	3.3	IESBA update	Note	Paper		10
	3.4	XRB environmental scan	Note	Paper		13
	3.5	Assurance scan	Note	Paper		22
10.45am	<i>Morning tea</i>					
11:15am	4	<u>ISA for Less Complex Entities</u>				
	4.1	Summary paper	Note	Paper	7	
	4.2	Issues paper	Discuss	Paper	11	
	4.3	Draft Exposure draft	Consider	Paper	14	
	4.4	Draft Consultation Document	Consider	Paper	199	
	4.5	Mapping: Requirements Part 11 to NZAS 1R	Note	Paper		24
12:15pm	5	<u>Review Standard on Service Performance Information</u>				
	5.1	Summary paper	Note	Paper	217	
	5.2	Key themes	Consider	Paper	219	
	5.3	Submissions	Note	Paper		75
	5.4	Focus Group Feedback	Note	Paper		90
12:45pm	<i>Lunch</i>					
1:30pm	6	<u>Update on ISO Sustainability Assurance by Graeme Drake</u>				
	6.1	Summary Paper – ISO Sustainability Assurance	Note	Paper	222	
2:15pm	7	<u>Sustainability Competence</u>				
	7.1	Summary Paper	Discuss	Paper	223	
	7.2	Analysis – Professional Accountants	Note	Paper		94

Est.Time	Item	Topic	Objective		Page	Supplementary
	7.3	Analysis – Non-Accountants	Note	Paper		105
3pm	8	<u>Supporting GHG emissions assurance</u>			KT	
	8.1	Summary Paper	Note	Paper	230	
3:15pm	<i>Afternoon Tea</i>					
3:30pm	9	<u>Public Interest Entity Amendments Consultation</u>			SW	
	9.1	Summary Paper		Paper	232	
	9.2	Issues		Paper	235	
	9.3	Submissions and other feedback		Paper		111
5pm	<u>Closing</u>					

Next Meeting:
17 October in Auckland

AGENDA ITEM NO. 3.1
Meeting date: 7 August 2024
Subject: NZAuASB Prioritisation schedule
Date: 25 July 2024
Prepared By: Misha Pieters

Action Required

For Information Purposes Only

Objective

1. The objective is for the Board to NOTE the supplementary papers including environmental scanning and DISCUSS the prioritisation schedule of the NZAuASB for 2024/25.

Background

2. We have continued to reflect on ways to incorporate environmental scans. We have rearranged the agenda, so the environmental scanning are supplemental papers to the NZAuASB's prioritisation plan for 2024/25.
3. Staff reflect what we believe to be relevant developments in updating the schedule and in the relevant agenda items.

Matters to Consider

4. We highlight:
 - a. The [FRC](#) has welcomed government legislation to modernise the regulatory toolkit. In the King's Speech, King Charles III noted that Bills will be brought forward to strengthen audit and corporate governance in the UK. This follows our previous update on Audit reform discussions in Australia. We will monitor developments and consider the implications for New Zealand. This has been added as domestic action.
 - b. Encouragement in the [Acuity magazine](#) for the XRB and AUASB to work together on a sustainability assurance framework going forward. The priority of this work is considered in the appendix.
 - c. The debate regarding audit firm rotation was highlighted in recent NBR articles. The IESBA has a post implementation review of the long association requirements, including audit firm rotation, planned to commence in 2026. Staff have not added any specific action for this 12 month period. Disclosure of audit firm tenure is an alternative to mandatory firm rotation.
 - d. IFAC has issued a [one-page summary](#) of what to expect from sustainability assurance. The summary recognises that modified opinions might be common in the first years of sustainability assurance and compares this to the first few years of the Sarbanes Oxley regime. We will be exploring this further with assurance practitioners during our upcoming ghg sandbox sessions and in developing collateral for our broader communications work.

Recommendation

5. We request feedback from the Board
 - a. On rearranging the agenda in this manner.
 - b. On the updates to the prioritisation schedule.

2024/25 Prioritisation Plan

Domestic Project	2024/25 planned action	Resource	Priority/effort	Key deliverable	Due
Review standard for service performance information	Analyse submissions and issue standard. Submissions received included in August agenda.	Available	Medium	Issue standard	Oct
ISA (NZ) for LCE	Issue exposure draft and finalise standard including chapter on service performance information Issues on August agenda	Available	High	Issue ED Issue standard	Oct By June
Monitor adoption of audit and review of service performance	Monitor developments, hold workshops, work with accounting team and issue guidance as needed Update on XRB initiative	Available	High	Issue guidance	Dec
Value of audit	Monitor audit reform in UK/Australia Explore audit quality	TBD	TBD	TBD	TBD
	Monitor inspection findings	Available	Medium	Report	Feb
Monitor and comms over mandatory GHG assurance	Monitor developments, hold workshops and issue guidance as needed Plan in Aug agenda	Available	High	Snapshots Insights and FAQs	Ongoing
	Explore user needs and value of adding to assurance reports	TBD	TBD	TBD	TBD
Limited versus reasonable assurance	Assist the market understand the spectrum of assurance, what limited assurance actually means and the value of assurance	To manage	High	Animation/video	Dec
XRB strategy for climate assurance – adoption of ISSA 5000/ISO or something else	Consider developing a white paper to consult on climate and or sustainability assurance in New Zealand as we monitor international developments and government policy decisions	Available	TBD	TBD	TBD
Competency requirements for sustainability assurance	Explore whether necessary to add requirements or issue guidance in Aug agenda	Available	TBD	TBD	TBD
Update standard setting policy based on developments in assurance over climate disclosures	Revise EG Au2 and update harmonisation/convergence policy	Available	Medium	Updated policy as appropriate	April
Māori engagement	Engage proactively to seek Māori views on relevant issues	To manage	TBD	TBD	
Digitisation	Standards navigator is live. Ongoing maintenance	To manage	TBD	TBD	
Explore assurance related issues related to Ngā pou o te kawa ora	Monitor developing XRB reporting framework and if and when appropriate, consider assurance related matters	To manage	Low	TBD	TBD
Technology	To monitor and respond if appropriate	To manage	TBD	TBD	TBD

IAASB

IAASB	2024/25 planned action	Resource	Priority /effort	Key deliverable	Due
Going concern revised standard	IAASB expect to approve in Dec 2024, and issue in March. Issue final updated standard in New Zealand by June 2025	Available	Medium	Standard	June 2025
Public Interest Entity track 2	IAASB expect to approve in Dec 2024, and issue in March. Issue NZ final standard by June 2025. NZ feedback on Aug agenda	Available	High	Standard	June 2025
Vision and roadmap for technology	Monitor developments and determine implications	Available	Medium	TBD	Dec 24
Reference framework model in relation to audit evidence	Monitor developments and finalisation of ISA 500 when determined by IAASB	Available	Low	Standard	TBD
Performance aspects in relation to responding to assessed risk and analytical procedures	Monitor developments	Available	Low	Standards	TBD
Narrow scope amendments from IESBA's use of experts	Consult on proposals (comment period to close July 2025)	Available	Low	Exposure draft	April
Explore issues on materiality in practice to inform international project to revise materiality standard	IAASB project to commence Jan 2025	Available	Medium		
Fraud standard (ISA (NZ) 240)	Monitor developments. IAASB expect to approve in March 2025 and issue in June. Adopt in New Zealand once issued (expected Sep 2025)	Available	High	Standard	TBD
ISSA 5000 Sustainability	IAASB expected to approve standard in Sept 2024. XRB yet to determine whether to adopt ISSA 5000	Available	Medium	TBD	June 2025
ISRE 2410 Interim Review Engagements	IAASB project commence April 2025. Consider XRB support for IAASB	TBD	TBD		
Participate in NSS meetings/regional groups/advisory groups/task forces/host international guests	IAASB membership maintained Participate and lead a discussion at NSS meeting.	Available	High		

IESBA

IESBA	2024/25 planned action	Resource	Priority/effort	Key deliverable	Due date
Sustainability ethics and independence revisions	IESBA expected to approve standard in Dec 2024 and issue in March 2025. Monitor developments and determine implications for XRB.	Available	High	Update PES 1	June 2025
Use of experts	IESBA expected to approve standard in Dec 2024 and issue in March 2025. Monitor developments and determine implications for XRB.	Available	High	Update PES 1	June 2025
Collective investment vehicles	Monitor IESBAs project on CIVs, pension funds and investment company complexes – ED expected in 2025	Available	Low	TBD	TBD
Profession agnostic independence standards for sustainability assurance not in scope of Part 5	TBD		TBD		
Post implementation review of non-compliance with laws and regulations (NOCLAR)	Participate in IESBA PIR	To manage	Medium	TBD	TBD
Participate in NSS meetings/regional groups/advisory groups/task forces/host international guests	Host IESBA members/staff Participate and lead a discussion at NSS meeting.	Available	High	TBD	TBD

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 4.1
Meeting date: 7 August 2024
Subject: ISA (NZ) for LCE
Date: 24 July 2024
Prepared By: BM

Action Required

For Information Purposes Only

Agenda Item Objectives

1. The objective of this agenda item is to:
 - a. CONSIDER international developments, in particular the maintenance of the standard;
 - b. CONSIDER changes to the developing exposure draft since the June meeting;
 - c. CONSIDER a first draft of a consultation document.

Background

2. Whilst we aimed to approve an exposure draft at this meeting, there are a couple of issues arising that necessitate slowing down the issuance of an exposure draft of the ISA (NZ) for LCE:
 - a. Delays in the Supplemental guidance from the IAASB. The IAASB has pushed out the publication of the majority of their supplemental guides to Q3, 2024. We were expecting these by June (Q2). These guides will address important topics for staff to consider, prior to issuing the exposure draft, such as additional guidance on the authority, first time adoption of the standard, and maintenance of the standard.
 - b. Maintenance of the standard. The IAASB are yet to confirm how they plan to maintain the ISA for LCE.
 - c. Other projects currently being undertaken by the XRB. These include:
 - workshops to obtain an understanding of key issues surrounding the reporting and audit of service performance information. (refer to agenda item 1). We need time to reflect on the issues, possible solutions and whether Part 11, that largely follows the principles of NZ AS 1 (Revised)¹ will be fit for purpose for the audit of service performance information (SPI) for less complex entities.
 - the feedback from the consultation of the ED of the Review standard for SPI- following the Board discussion on the feedback received (refer agenda item 5) we

¹ NZ AS 1 (Revised) *The Audit of Service Performance Information*

will consider if any issues apply to audits of SPI of less complex entities, and how those issues would impact the drafting at Part 11.

Matters to Consider

International developments

Supplemental Guidance

3. In July 2024, the IAASB issued [Auditor Reporting Supplemental Guidance](#). This guidance provides assistance for auditors about modifications to the auditor's report when using the ISA for LCE. It also includes information on using emphasis of matter and other matter paragraphs, reporting on other information, and reporting on a material uncertainty related to going concern. The guidance features eight illustrative auditor's reports, including examples of adverse opinions, disclaimer of opinion, and opinions when there is a material uncertainty related to going concern. From our initial reading of this guidance, it will be useful for NZ. We will look to develop a NZ version in due course – with NZ spelling and references to the Professional and Ethical Standards (PES) and SPI, as required.
4. The guidance does not help with the OAG's need to customise audit reports. The guide refers to law and regulation as the only means possible of amending the specified format and content of the audit report. Therefore, we continue to recommend paragraph NZ9.4.1.A, as agreed at the June meeting, to enable the Auditor General's auditing standards to amend the specified format and content of the audit report in ISA (NZ) for LCE.

Update on other countries

5. Following the previous board meeting, we continue to monitor countries who are and who are not looking to adopt the ISA for LCE. This is partly reflected in our consultation document as well. There are no issues arising from our monitoring to bring to the Board's attention.

Maintenance of the ISA for LCE

6. As noted in the previous board meeting, a key risk for the XRB is how the ISA for LCE will be maintained by the IAASB. To enable adoption, the IAASB committed to an initial period of stability of 3 years, before any changes are made to realign with recent revisions to the ISAs.
7. The ongoing maintenance of the standard following this initial period of stability is an important consideration for the XRB before we commit to adopting this standard. One of the concerns emerging regarding the adoption of the ISA for LCE is the perception of a two-tier audit environment. The way in which the standard is maintained globally may impact on these perceptions. Because of this, we have included the topic of maintenance of the standard in the draft consultation document and recommend seeking views from stakeholders on this issue.
8. The IAASB is yet to communicate the way it will maintain the ISA for LCE after the initial stable period. The IAASB has stated that in deciding the way forward the ISA for LCE must remain up to date and, to the greatest extent possible, consistent with the ISAs. Possible options include:
 - a. periodically, for example every 3 – 5 years, which would mean the amended ISA for LCE is applicable some years after the ISAs are amended;
 - b. developed and consulted on at the same time as revising or consulting on a new ISA, and with the same application date as revisions to the ISAs;

- c. developed and consulted shortly after the ISAs are amended, meaning a time lag between the application in the ISAs and the ISA for LCE.
9. If the XRB agrees to adopt the ISA for LCE in New Zealand, staff do not recommend that the XRB should amend the standard ahead of the IAASB updating the standard.

10. We seek the Board's views on the maintenance of the standard.

Exposure Draft

11. Further amendments made to Part 11 and the rest of the standard since the June meeting are discussed in the Issues paper at agenda item 4.2. However, we may need to reflect on this again following the workshops and outcome noted in agenda item 1.
12. While the draft Part 11 is based on NZ AS 1 (Revised), there are areas (such as materiality requirements or the requirements to respond to the risk of material misstatement (ROMM) at the service performance information (SPI) level) where we may need to add to/tailor the requirements in Part 11.
13. Matters to discuss are outlined in the issues paper at agenda item 4.2 and include:
- a. Amendments to the materiality requirements in Part 11.
 - b. Any other comments on Part 11.
 - c. Modifications to the ISA (NZ) for LCE arising from compelling reasons.
 - d. Conforming amendments arising from the ISA (NZ) for LCE.

14. We seek the Board's views on the issues identified in agenda item 4.2, the changes made to Part 11 since the June meeting, and the proposed application date.

Consultation Document

15. The draft consultation document at agenda item 4.4 has been developed based on key issues that have been discussed throughout the development of the exposure draft. It covers:
- a. Should we adopt the ISA for LCE in New Zealand? – explores the benefits and potential perception issues, and discussion on the maintenance of the standard.
 - b. Applicability of the standard in New Zealand – Provides an overview of the Authority of the standard, and proposals for a specific prohibition on FMC HLPAs and not having a quantitative threshold.
 - c. Audit of Service Performance Information in the ISA (NZ) for LCE. Provides an overview of Part 11, key aspects where requirements have been tailored, recognising the known issues around service performance information.
 - d. New Zealand specific amendments to the ISA (NZ) for LCE – Providing a summary of changes made to the ISA for LCE based on the compelling reasons test.
 - e. Application date
 - f. Other matters

16. We seek the Board's views on the draft consultation document.

Timeline

17. Given the issues mentioned in the Background section, we will continue to reflect on those issues and refine the exposure draft and issues for consultation. The consultation document on the ISA (NZ) for LCE, could also be used to inform our work on the project looking at service performance information reporting and assurance by seeking out further feedback.
18. We may aim for approval of the package at the October 2024 meeting, or at a subsequent meeting.
19. The IAASB date for application of the ISA for LCE is for periods beginning on or after 15 December 2025 – which means December 2026 balance dates. While we are slowing down the issue of the ED, we still consider that it is possible to complete and issue a New Zealand standard by June 2025. We continue to aim for an application date that aligns with the international date.
20. To recognise that this is a voluntary standard we have added a paragraph into the Authority at NZA.5., which reads

NZA.5. The XRB permits the voluntary application of the ISA (NZ) for LCE in specific circumstances. Auditors may voluntarily adopt this standard:

 - (a) *On or after the mandatory date, or early adoption accounting period, as defined in the Commencement and Application section of this standard; and*
 - (b) *Where the auditor determines that the audit engagement can be undertaken using the ISA (NZ) for LCE in accordance with Part A of this standard. (Ref: Para. 3.2.9., 4.3.1., 6.5.1., 8.5.1.).*
21. This paragraph pulls together the mandatory application date paragraphs, the authority, and provides clarity that this is a voluntary standard. Staff propose that this detail is replicated in the proposed conforming amendments to XRB Au1.

22. We seek the Boards views on the proposed timeline and paragraph NZA.5.

Material Presented

Agenda item 4.1	Board Meeting Summary Paper
Agenda item 4.2	Issues Paper
Agenda item 4.3	Draft exposure draft
Agenda item 4.4	Draft consultation paper
Supplementary Agenda item 4.5	Mapping between Part 11 and NZ AS 1 (Revised)

ISA (NZ) for LCE: Issues Paper

1. This paper highlights key issues to discuss in refining the exposure draft.
2. The next iteration of the exposure draft is located at agenda item 4.3. Track changes have been applied to highlight modifications made to Part 11 since the June NZAuASB meeting discussions. Additionally, for the rest of the standard, track changes indicate where the standard has been amended from the international ISA for LCE.
3. Staff have re-read each paragraph in Part 11 and considered its flow and content, including its overall mapping to NZ AS 1 (Revised) and internal consistency within the ISA (NZ) for LCE. We have carefully considered each paragraph where additions have been made or requirements reworded. We have created another mapping document to illustrate similarities and differences between NZ AS 1 (Revised) *The Audit of Service Performance Information* and Part 11. This is at supplementary agenda item 4.5. However, we continue to hear frustrations in the system between auditors and preparers, so also need to bear in mind whether any of these challenges stem from the approach in NZ AS 1 (Revised) and avoid replicating issues in the LCE environment.
4. In summary we have made the following updates to the exposure draft:
 - (a) The preface has been amended to refer to SPI at the start of the standard. We have also ensured that the preface adequately addresses Public Sector audits. (Ref: para. NZP.1., NZP.18.)
 - (b) The authority has been amended arising from the decision to specifically prohibit FMC HLPAs reporting entities and not add a quantitative threshold. (Ref: para. A.1. (c) (iii) and (iv) and NZA.4.)
 - (c) The objective of Part 11 has been amended to align with NZ AS 1 (Revised). (Ref: para. 11.11.1.)
 - (d) Expanded EEM on Assertion Level risks at para. 11.7.2.
 - (e) Added reference to the risk of bias in the EEM at para. 11.8.1.
 - (f) Clarified the documentation requirements at para. 11.21.1.

Materiality

5. Staff have further considered this section in light of the drafting principle that the ISA for LCE is clear, understandable and concise.
 - (a) Firstly, to avoid confusion that may arise between the terms significant and material, we recommend moving the requirement, at 11.6.1(a) that the auditor “*determine which elements/aspects of service performance are significant or important to intended users*”, to EEM.

The new first paragraph in the EEM at 11.6.1, is based on NZ AS 1 (Revised) para. A52, which states:

“In considering or determining the materiality for service performance information, the auditor may firstly determine which elements/aspects of service performance are significant or important to intended users, i.e., the significant elements/aspects of service performance. Having identified those, the auditor may then consider or determine what are the material performance measures and/or descriptions that

measure performance in those significant elements/aspects of service performance.”

- (b) Secondly, the initial drafting of the second bullet point is slightly unclear “*Determine materiality considerations and/or materiality for service performance information*” – one could question how do you determine and consider materiality at the same time? To avoid confusion, we have redrafted this to read “*Consider materiality for qualitative service performance information; and/or Determine materiality for quantitative service performance information.*”
- (c) Thirdly in the initial drafting, it was unclear as to whether the auditor needs to set performance materiality. Therefore, we have clarified this by adding a requirement that the auditor shall “*For quantitative service performance information, determine performance materiality as applicable in the circumstances.*”. EEM has been added on this matter as well. This leaves it to the auditor to determine whether or not to determine performance materiality. It also provides clarity, rather than leaving the auditor to guess whether or not they need to determine/document performance materiality in the audit of service performance information.

- 6. **We seek the Board’s views on the *materiality* requirements (section 11.6 of the ISA (NZ) for LCE, agenda item 4.3)**
- 7. **We seek any other comments on the rest of Part 11.**

Modifications to the ISA (NZ) for LCE arising from compelling reasons

- 8. Given that the NZAuASB has previously identified the compelling reasons to amend the ISAs (NZ) for various requirements throughout the ISAs (NZ), we have carried across those same amendments into the ISA (NZ) for LCE.
- 9. Broadly we have made amendments to the ISA (NZ) for LCE in relation to the following:
 - Responsibilities for the financial statements being those of governance rather than management. This adjusts requirements relating to the engagement letter, auditor’s report, and written representations.
 - Adding reference to the specific NZ financial reporting frameworks, and the NZ standard setters (i.e. NZAuASB/NZASB/XRB).
 - Adding reference to the New Zealand Professional and Ethical Standards, and the requirement to refer to them in the auditor’s report.
 - Timing of the going concern assessment, being 12 months from the date of the auditor’s current report.
 - Requiring, when applicable, the auditor to discuss facts which become known after the financial statements have been issued within a reasonable period of time with management and, where appropriate, those charged with governance.
 - Guidance for the auditor to communicate with management if the auditor will intend to rely on a written public statement.
 - Adding guidance that comparative financial statements are not included in financial statements prepared under NZ generally accepted accounting practice.
 - Delete reference to checks/cheques in the definition of Accounting Records – as these are no longer used in New Zealand, they are unlikely to be applicable to less complex entities.
- 10. To undertake this task, we reviewed each ISA (NZ) auditing standard for those types of paragraphs prefixed with “NZ” or which have been amended for NZ circumstances. For each of those

Agenda item 4.2

paragraphs, we then considered whether they should be included in the ISA (NZ) for LCE, i.e. are they relevant for an audit of a less complex entity. When making the necessary modifications, we also considered the drafting and alignment principles set by the IAASB. In keeping with current practice, each amended paragraph or amended EEM in the ISA (NZ) for LCE is prefixed by “NZ”. Amended requirement paragraphs have “[Amended by the NZAuASB]” added to also indicate that the paragraph differs from its international equivalent.

11. This topic is also covered in our consultation document.

12. Does the Board agree with the logic to carry forward amendments made due to compelling reasons in the ISAs (NZ) into the ISA (NZ) for LCE, where applicable? Does the Board have any comments on the added NZ paragraphs?

Conforming amendments arising from the ISA (NZ) for LCE

13. We have reviewed the proposed conforming amendments from the IAASB (located at the back of the standard) and considered the applicability in the NZ context. Arising from this review, we propose that conforming amendments are made to the standards listed below. These are shown as track changes at the back of the standard at agenda item 4.3.

- XRB Au1, *Application of Auditing and Assurance Standards*
- PES 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)*
- PES 3, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*
- PES 4, *Engagement Quality Reviews*
- ISAE (NZ) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*
- ISRE (NZ) 2400, *Review of Historical Financial Statements Performed by an Assurance Practitioner who is Not the Auditor of the Entity*

14. Broadly, these amendments either add reference to the ISA (NZ) for LCE in the standards above or, in the case of ISRE (NZ) 2400, remove the reference to the ISAs (NZ) and instead add a general reference to auditing standards issued by the XRB.

15. We will also take the opportunity to update IAPN 1000, *Special Considerations in Auditing Financial Instruments*, to include the amendments arising from the ISA for LCE and the ISA (NZ) 315 (Revised 2019) revisions which were included in the IAASB 2021 Handbook. We have contacted the IAASB on this IAPN, and they have no further immediate plans to update this IAPN, so it still does not include updates from ISA 540 (Revised). As changes to IAPN do not get gazetted look at updating this practice note when we come to finalise the standard, or in due course.

16. If the ISA (NZ) for LCE is issued in NZ, we are considering splitting the conforming amendments section into a standalone standard – similar to how the conforming amendments arising from ISA (NZ) 600 (Revised) were issued as a standalone standard. Why would we do this? Partly because it would make the standard easier to digitise. Also, over time, conforming/consequential amendments become less relevant to the users of the standard. And having them in a separate standard prevents them from cluttering the core standard.

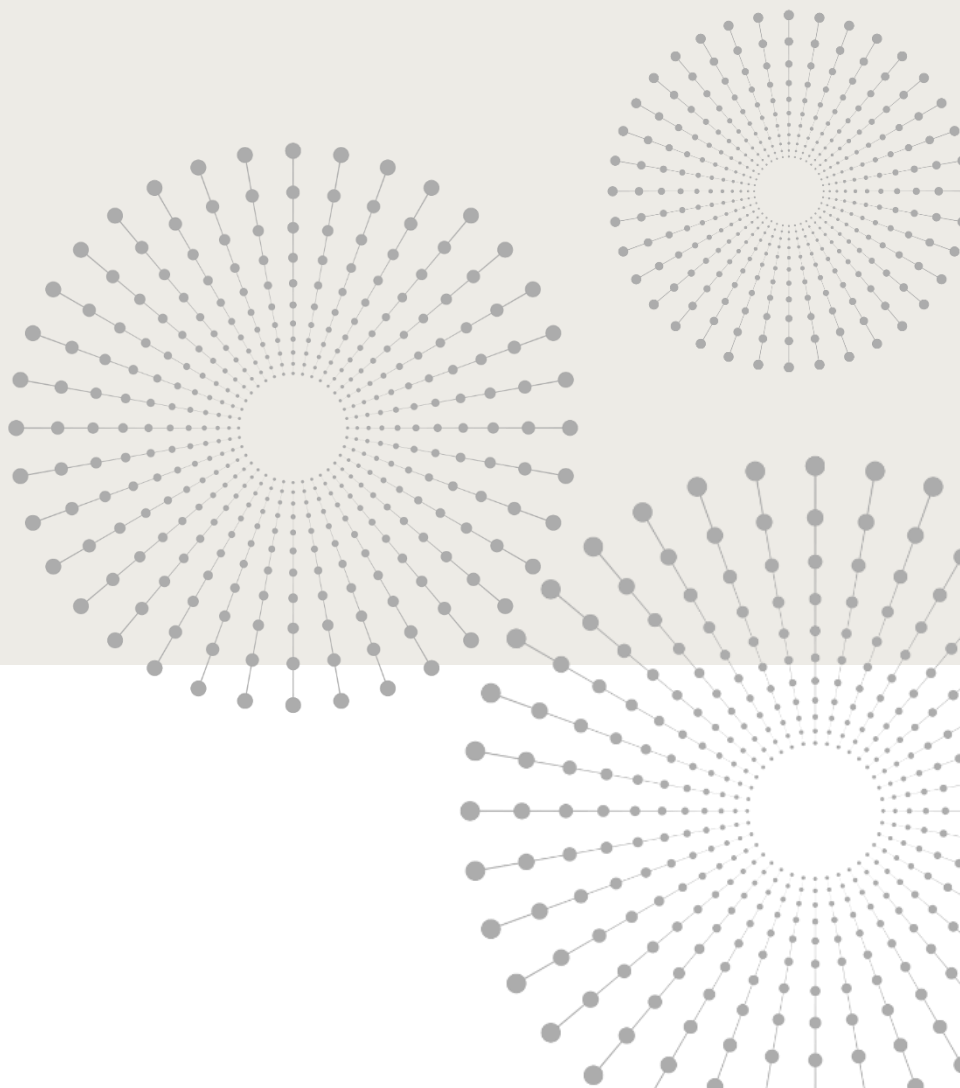
17. Does the Board have any comments on the proposed conforming amendments?

International Standard on Auditing (New Zealand) For Audits of Financial Statements of Less Complex Entities

The ISA (NZ) for LCE

Exposure Draft

Submissions close **DATE**



2024



THE INTERNATIONAL STANDARD ON AUDITING (NEW ZEALAND) FOR AUDITS OF FINANCIAL STATEMENTS OF LESS COMPLEX ENTITIES

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THE INTERNATIONAL STANDARD ON AUDITING **(NEW ZEALAND)** FOR AUDITS OF FINANCIAL STATEMENTS OF LESS COMPLEX ENTITIES

~~(Effective for audits of financial statements of less complex entities for periods
Beginning on or after December 15, 2025)~~

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Commencement and application

When standard takes effect (Section 27 Financial Reporting Act 2013)

1. This standard takes effect on the 28th day after the date of its publication under the Legislation Act 2019¹.

Accounting period in relation to which standards commence to apply (section 28 Financial Reporting Act 2013)

2. The accounting periods in relation to which this standard commences to apply are:
 - (a) for an **early adopter**, those accounting periods, following and including, the **early adoption accounting period**.
 - (b) for any other auditor, those accounting periods following, and including, the first accounting period that begins on or after the **mandatory date**.

3. In paragraph 2:

early adopter means an auditor that applies this standard for an early adoption accounting period.

early adoption accounting period means the accounting period:

- (a) that begins before the mandatory date but has not ended or does not end before this standard takes effect (and to avoid doubt, that period may have begun before this standard takes effect); and
- (b) for which the early adopter:
 - (i) first applies this standard for an audit engagement of a less complex entity; and
 - (ii) discloses in the auditor's report for that accounting period that this standard has been applied for that period.

mandatory date means [TBC].

¹ The standard was published on [Date]

History of amendments

Table of pronouncements – ISA (NZ) for LCE

This table lists the pronouncements establishing and amending the ISA (NZ) for LCE.

<u>Pronouncements</u>	<u>Date approved</u>	<u>Mandatory date</u>
<u>International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities</u>	<u>TBC</u>	<u>[TBC]</u>

Preface to the ~~ISA for LCE~~ISA (NZ) for LCE

P.1. ~~[Amended by the NZAuASB]~~

~~NZP.1.~~ This standard (i.e., the ISA ~~(NZ)~~ for LCE) has been designed to achieve reasonable assurance about whether the ~~general purpose~~ financial statements, ~~and inclusive of service performance information, where relevant,~~ as a whole are free from material misstatement, whether due to fraud or error, for audits of ~~general purpose financial statements, and inclusive of service performance information, financial statements~~ of less complex entities (LCEs) in the private and public sectors. The standard has been developed to reflect the nature and circumstances of an audit of the ~~service performance information, where relevant, and the~~ financial statements of an LCE and result in the consistent performance of a quality audit engagement. This standard is premised on the basis that the firm is subject to ~~Professional and Ethical Standard 3~~ISQM 1² or to national requirements that are at least as demanding. A quality audit engagement is achieved by planning and performing the engagement and reporting on it in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objective of this standard involves exercising professional ~~judgment~~judgement and maintaining professional ~~skepticism~~scepticism.

P.2. This standard is written in the context of an audit of a complete set of general purpose financial statements³ of an LCE as contemplated in Part A. It 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, only if the entity is an LCE as set out in Part A.

P.3. When an audit engagement is undertaken using this standard, the International Standards on Auditing ~~(New Zealand)~~ do not apply to the engagement.

P.4. Part A sets out the authority for determining the appropriate use of the ISA ~~(NZ)~~ for LCE. Decisions about the required or permitted use of this standard, including descriptions of the type of entities for which an audit in accordance with this standard may be used rest with legislative and regulatory authorities or relevant local bodies with standard-setting authority.

P.5. If this standard 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~~ISA (NZ) for LCE in the auditor's report.

P.6. This standard does not override local law or regulation that governs audits of financial statements in a particular jurisdiction. The ~~ISA for LCE~~ISA (NZ) for LCE does not address the responsibilities of the auditor that may exist in legislation or regulation. Such responsibilities may differ from those established in this standard and it is the responsibility of the auditor to ensure compliance with all relevant legal, regulatory, or professional obligations.

The Applicable Financial Reporting Framework

P.7. The financial statements subject to audit are those of the entity, prepared by management of the entity with oversight from those charged with governance. Law or regulation may establish the responsibilities of management, and those charged with governance, in relation to financial reporting. This standard does not impose responsibilities on management or those charged with governance and does not override law or regulation that govern their responsibilities. However, an audit in accordance with this standard is conducted on the premise that management, and

² Professional and Ethical Standard (PES) 3, *Quality Management for Firms that Perform Audits or Reviews for Financial Statements, or Other Assurance or Related Services Engagements*

³ [NZ] In accordance with paragraph NZP.16A., references in this standard to *Financial Statements* include, where relevant, *Service Performance Information* and *Entity Information*, when an auditor is applying Part 11.

where appropriate, those charged with governance have acknowledged certain responsibilities that are fundamental to the conduct of the audit. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

NZP.7.A. In New Zealand, those charged with governance generally have responsibility for ensuring an entity meets its legal obligations in relation to the preparation of the financial statements, often delegating the process of financial reporting to management, while retaining ultimate responsibility. Auditors shall use professional judgement and knowledge of New Zealand's legal and governance standards to assess if this standard's requirements pertain to management, those charged with governance, or both. In this ISA (NZ) for LCE, "management" should be read hereafter as "management and, where appropriate, those charged with governance."

Management's and Those Charged with Governance's Responsibilities for Preparation of the Financial Statements

The extent of management's responsibilities, or the way that they are described, may differ across jurisdictions. While there may be differences in the extent of those responsibilities or how they are described, an audit in accordance with this standard is conducted on the premise that management, and where appropriate, those charged with governance, have acknowledged and understood that they have responsibility:

- *For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant, their fair presentation;*
- *For such internal control as management, and where appropriate, those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and*
- *To provide the auditor with unrestricted access to all information of which they are aware that is relevant to the preparation of the financial statements, additional information the auditor may request, and unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.*

- P.8. The applicable financial reporting framework often encompasses financial reporting standards established by an ~~authorized~~authorised or ~~recognized~~recognised standard setting organization, or legislative or regulatory requirements.
- P.9. The requirements of the applicable financial reporting framework determine the form and content of the financial statements. Although the framework may not specify how to account for or disclose all transactions or events, the framework ordinarily embodies sufficiently broad principles that can serve as a basis for developing and applying accounting policies consistent with the framework's concepts underlying the requirements.
- P.10. Some financial reporting frameworks are fair presentation frameworks, while others are compliance frameworks. This standard covers both frameworks. The term "fair presentation framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:
- (a) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
 - (b) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.

[NZ] The Examples of financial reporting requirements that are designed to achieve fair presentation in New Zealand include the following issued by the New Zealand Accounting Standards Board:

- New Zealand equivalents to International Financial Reporting Standards (NZ IFRS)
- New Zealand equivalents to IFRS Reduced Disclosure Regime (NZ IFRS RDR);
- Public Benefit Entity Standards (PBE Standards)
- Public Benefit Entity Standards Reduced Disclosure Regime (PBE Standards RDR);
- Reporting Requirements for Tier 3 Public Sector Entities (Tier 3 (PS) Standard);
- Reporting Requirements for Tier 3 Not-for-Profit Entities (Tier 3 (NFP) Standard).

Examples of financial reporting requirements that only require compliance with the requirements (compliance frameworks) in New Zealand include the following issued by the New Zealand Accounting Standards Board:

- Reporting Requirements for Tier 4 Public Sector Entities (Tier 4 (PS) Standard);
- Reporting Requirements for Tier 4 Not-for-Profit Entities (Tier 4 (NFP) Standard).

An Audit of Financial Statements

- P.11. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. As the basis for the auditor’s opinion, this standard requires the auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error.
- P.12. Reasonable assurance is a high level of assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor’s opinion being persuasive rather than conclusive.

Inherent Limitations of an Audit

Audit risk is a function of the risks of material misstatement and detection risk. The assessment of risks of material misstatement is based on audit procedures to obtain information necessary for that purpose and evidence obtained throughout the audit. The assessment of risks of material misstatement is a matter of professional ~~judgment~~judgement, rather than a matter capable of precise measurement.

Because of the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with this standard. Accordingly, the subsequent discovery of a material misstatement resulting from fraud or error does not by itself indicate a failure to conduct an audit in accordance with this standard. However, the inherent limitations of an audit are not a justification for the auditor to be satisfied with less than persuasive audit evidence.

Format of the ~~ISA for LCE~~ISA (NZ) for LCE

P.13. [Amended by the NZAuASB]

NZP.13. The ~~ISA for LCE~~ISA (NZ) for LCE includes:

- (a) Part A, which sets out the authority for determining the appropriate use of the ~~ISA for LCE~~ISA (NZ) for LCE.
- (b) Part 1, which sets out the fundamental concepts, general principles and overarching requirements to be applied throughout the audit.
- (c) Part 2, which sets out the general requirements for audit evidence and documentation, as well as the overall objective of the audit.
- (d) Part 3, which sets out the auditor's and engagement partner's obligations and responsibilities for quality management in an audit of an LCE.
- (e) Parts 4 to 9, which follow the flow of an audit engagement, and set out the detailed requirements for the audit. Each of these Parts also includes specific communication and documentation requirements as necessary.
- (f) Part 10, which sets out the special considerations that apply to an audit of group financial statements.
- (g) Part 11, which sets out the considerations that apply to an audit of service performance information.
- (gh) Appendices, which include the glossary of terms used in this standard, assertions, an illustrative engagement letter and an illustrative representation letter, as well as other relevant supporting materials for implementation of the requirements within this standard.

P.14. [Amended by the NZAuASB]

NZP.14. The content of Parts 1–~~110~~ includes: Parts 1–~~10~~1

- (a) Introductory material in a separate box setting out the content and scope of that Part (but does not create any additional obligations for the auditor).
- (b) Objective(s), which link the requirements of that Part and the overall objective of the audit.
- (c) Requirements to be met, except where the requirement is conditional, and the condition does not exist. Requirements are expressed using "shall."
- (d) Essential explanatory material (EEM) designed to provide further explanation relevant to a sub-section or a specific requirement. All EEM is presented in italics within separate blue boxes. There are two types of EEM: general introductory EEM that explains the context of the section that follows, and EEM specific to the requirement directly above it.

Certain requirements and EEM are only applicable when there are engagement team members other than the engagement partner. Such requirements and EEM are presented in a box with the header "Considerations When There Are Members of the Engagement Team Other Than the Engagement Partner".

P.15. Definitions, describing the meanings attributed to certain terms for the purpose of this standard, 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.

P.16. For the purposes of this standard, the use of "LCE" or "entity" also refers to a group (i.e., where the audit is an audit of group financial statements).

NZP.16A. For the purposes of this standard, the use of “financial statements” also refers to “service performance information” and where relevant “entity information” (i.e., where the audit is an audit of financial statements and service performance information and, where relevant, entity information).

Non-Authoritative Support Materials

P.17. [Amended by the NZAuASB]

NZP.17. The ~~IAASB~~~~IRB~~ may issue ~~Staff publications or other~~ non-authoritative material to support the implementation of the ~~ISA for LCE~~ISA (NZ) for LCE.

Public Sector Entities

P.18. [Amended by the NZAuASB]

NZP.18. This standard is relevant to engagements in the public sector, when the considerations set out in the Authority in Part A apply. The public sector auditor’s responsibilities, however, may be affected by the audit mandate, or by obligations on public sector entities arising from law, regulation or other authority (such as ministerial directives, government policy requirements, or resolutions of the legislature), which may encompass a broader scope than an audit of financial statements in accordance with this standard. These additional responsibilities are not dealt with in this standard. They may be dealt with in the Auditor-General’s Auditing Standards or in other guidance developed by the Auditor-General, ~~pronouncements of the International Organization of Supreme Audit Institutions or national standard setters, or in guidance developed by public sector audit agencies.~~

P.19. [Amended by the NZAuASB]

NZP.19. The applicable financial reporting framework used by a public sector entity is determined by the legislative and regulatory frameworks relevant to each jurisdiction or within each geographical area. Matters that may be considered in the entity’s application of the applicable financial reporting requirements, and how it applies in the context of the nature and circumstances of the entity and its environment, include whether the entity applies a full accrual basis of accounting or a cash basis of accounting in accordance with the ~~International~~ Public Sector PBE Accounting Standards issued by the New Zealand Accounting Standards Board, or a hybrid.

P.20. Ownership of a public sector entity may not have the same relevance as in the private sector because decisions related to the entity may be made outside of the entity as a result of political processes. Therefore, management may not have control over certain decisions that are made. Matters that may be relevant include understanding the ability of the entity to make unilateral decisions, and the ability of other public sector entities to control or influence the entity’s mandate and strategic direction.

P.21. When appropriate, additional considerations specific to public sector entities have been included in EEM.

A. Authority of the ISA (NZ) for Audits of Financial Statements of Less Complex Entities

Content of this Part

Part A sets out the Authority for determining the appropriate use of the ~~ISA for LCE~~ISA (NZ) for LCE.

The ~~ISA for LCE~~ISA (NZ) for LCE is designed to enable the achievement of the overall objectives of the auditor, given the typical nature and circumstances of an LCE as described in this Part. There are limitations to the use of the ~~ISA for LCE~~ISA (NZ) for LCE that are designated into three categories: specific prohibitions, qualitative characteristics, and quantitative thresholds. Part A also describes the responsibilities for legislative or regulatory authorities or relevant local bodies with standard-setting authority to support the appropriate use of this standard. The use of “LCE” or “entity” also refers to a group (i.e., where the audit is an audit of group financial statements).⁴

The requirements in this ~~ISA for LCE~~ISA (NZ) for LCE have been designed to be proportionate to the typical nature and circumstances of an audit of an LCE (i.e., they do not address complex matters or circumstances). If the ~~ISA for LCE~~ISA (NZ) for LCE is used for an audit outside the intended scope of this standard, compliance with the requirements of the ~~ISA for LCE~~ISA (NZ) for LCE will not be sufficient for the auditor to obtain sufficient appropriate audit evidence to support a reasonable assurance opinion.

The Supplemental Guidance for the Authority of the Standard (the Authority Supplemental Guide) provides further guidance for legislative or regulatory authorities or relevant local bodies with standard-setting authority when addressing their respective responsibilities as described in this Part. In addition, the Authority Supplemental Guide further explains matters that may be relevant for firms and auditors in determining whether the use of the ~~ISA for LCE~~ISA (NZ) for LCE is appropriate.

Limitations for Using the ~~ISA for LCE~~ISA (NZ) for LCE

Limitations for using the ~~ISA for LCE~~ISA (NZ) for LCE are designated into three categories:

- *Specific classes of entities for which the use of the ~~ISA for LCE~~ISA (NZ) for LCE is prohibited (i.e., specific prohibitions);*
- *Qualitative characteristics that describe an LCE, and if not exhibited by an entity would ordinarily preclude the use of the ~~ISA for LCE~~ISA (NZ) for LCE for the audit of the financial statements of that entity; and*
- *Quantitative thresholds to be determined by legislative or regulatory authorities or relevant local bodies with standard-setting authority in each jurisdiction.*

In determining the appropriate use of the ~~ISA for LCE~~ISA (NZ) for LCE, all three categories are to be considered.

⁴ A “group” is a reporting entity for which group financial statements are prepared and “group financial statements” are financial statements that include the financial information of more than one entity or business unit through a consolidation process. The term “consolidation process” as used in the ISA (NZ) for LCE is not intended to have the same meaning as “consolidation” or “consolidated financial statements” as defined or described in financial reporting frameworks. Rather, the term “consolidation process” refers more broadly to the process used to prepare group financial statements. The Glossary of Terms (**Appendix 1**) describes the meanings attributed to certain terms for the purpose of the ISA (NZ) for LCE, including the meaning of group and group financial statements.

Specific Prohibitions

Paragraph A.1. sets out the classes of entities for which the use of this standard is specifically prohibited.

- A.1. The ~~ISA for LCE~~ISA (NZ) for LCE shall not be used if:
- (a) Law or regulation prohibits the use of the ~~ISA for LCE~~ISA (NZ) for LCE or specifies the use of auditing standards other than the ~~ISA for LCE~~ISA (NZ) for LCE for the audit of the financial statements in that jurisdiction.
 - (b) The entity is a listed entity.
 - (c) The entity falls into one of the following classes:
 - (i) An entity one of whose main functions is to take deposits from the public;
 - (ii) An entity one of whose main functions is to provide insurance to the public;
 - ~~(NZ iii) It is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” than other FMC reporting entities under section 461K of the Financial Markets Conduct Act 2013;~~
 - ~~(NZ iv) is an FMC reporting entity or a class of FMC reporting entities that is considered to have a “higher level of public accountability” by a notice issued by the Financial Markets Authority (FMA) under section 461L(1)(a) of the Financial Markets Conduct Act 2013; or~~
 - ~~(viii) A class of entities where use of the ~~ISA for LCE~~ISA (NZ) for LCE is prohibited for that specific class of entity by a legislative or regulatory authority or relevant local body with standard-setting authority in the jurisdiction.~~
 - (d) The audit is an audit of group financial statements (group audit) and:
 - (i) Any of the group’s individual entities or business units meet the criteria as described in paragraph A.1.(b) or A.1.(c); or
 - (ii) 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 (e.g., attending a physical inventory count or physically inspecting assets or documents).

A single legal entity may be ~~organized~~organised with more than one business unit, for example, a company with operations in multiple locations, such as a store with multiple branches. When those business units have characteristics such as separate locations, separate management, separate general ledger and the financial information is aggregated in preparing the single legal entity’s financial statements, such financial statements meet the definition of group financial statements because they include the financial information of more than one entity or business unit through a consolidation process.

In some cases, a single legal entity may configure its information system to capture financial information for more than one product or service line for legal or regulatory reporting or other management purposes. In these circumstances, the entity’s financial statements are not group financial statements because there is no aggregation of the financial information of more than one entity or business unit through a consolidation process. Further, capturing separate information (e.g., in a sub-ledger) for legal or regulatory reporting or other management purposes does not create separate entities or business units (e.g., divisions) for purposes of this ~~ISA for LCE~~ISA (NZ) for LCE.

Component Auditors

A component auditor is an auditor who performs audit work related to a component⁵ for purposes of the group audit. A component auditor is a part of the engagement team for a group audit. Component auditors may be from a network firm, a firm that is not a network firm, or the group auditor's firm (e.g., another office within the group auditor's firm).

In some circumstances, the group auditor may perform ~~centralized~~centralised testing on classes of transactions, account balances or disclosures, or may perform audit procedures related to a component. In these circumstances, the group auditor is not considered a component auditor.

Part 3 contains requirements in relation to engagement quality, including relevant ethical requirements, and the direction and supervision of the members of the engagement team, and the review of their work.

- A.2. The classes in paragraph A.1.(a) (b) and (d) are outright prohibitions and cannot be modified. Legislative or regulatory authorities or relevant local bodies with standard-setting authority can modify each class described in paragraph A.1.(c) but a class cannot be removed.

A.1.(c) sets out some classes of entities that may exhibit public interest characteristics. Entities that have public interest characteristics could embody a level of complexity in fact or appearance and are specifically prohibited from using the ~~ISA for LCE~~ISA (NZ) for LCE. Modifications can be made by adding a class of entities to the list of prohibited entities, permitting specific sub-sets within a class to be able to use this standard or using quantitative thresholds to prohibit use of this standard. Legislative or regulatory authorities or relevant local bodies with standard-setting authority may subsequently remove or amend modifications that they have made.

Qualitative Characteristics

The requirements in this ~~ISA for LCE~~ISA (NZ) for LCE have been designed to be proportionate to the typical nature and circumstances of an audit of an LCE.

The ~~ISA for LCE~~ISA (NZ) for LCE has not been designed to address:

- Complex matters or circumstances relating to the nature and extent of the entity's business activities, operations and related transactions and events relevant to the preparation of the financial statements.
- Topics, themes and matters that increase, or indicate the presence of, complexity, such as those relating to ownership of the entity, corporate governance arrangements of the entity, or policies, procedures or processes established by the entity.

Also, the ~~ISA for LCE~~ISA (NZ) for LCE does not include any requirements addressing:

- Procedures or matters typically relevant to listed entities, including reporting on segment information or key audit matters.
- When the auditor intends to use the work of internal auditors, as this would ordinarily not be applicable to an audit of an LCE.
- When the auditor intends to use a report provided by a service auditor of a service organization 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.

⁵ A component is an entity, business unit, function or business activity, or some combination thereof, determined by the group auditor for the purposes of planning and performing audit procedures in a group audit.

- A.3. The following list describes characteristics of an LCE for the purpose of determining the appropriate use of the ~~ISA for LCE~~ISA (NZ) for LCE. The list is not exhaustive nor intended to be absolute (including numerical indicators), and other relevant matters may also need to be considered. Each of the qualitative characteristics may not, on its own, be sufficient to determine whether the ~~ISA for LCE~~ISA (NZ) for LCE is appropriate or not in the circumstances. Therefore, the matters described in the list are intended to be considered both individually and in combination. For the purpose of group audits, these considerations shall apply to both the group and each of its individual entities and business units.

Business Activities, Business Model & Industry	<p>The entity's business activities, business model, or the industry in which the entity operates, do not give rise to significant pervasive business risks.</p> <p>There are no specific laws or regulations that govern the business activities that add complexity (e.g., prudential requirements).</p> <p>The entity's transactions result from few lines of business or revenue streams.</p>
Organizational Structure and Size	<p>The organizational structure is relatively straightforward, with few reporting lines or levels and a small key management team (e.g., 5 individuals or less).</p>
Ownership Structure	<p>The entity's ownership structure is straightforward and there is clear transparency of ownership and control, such that all individual owners and beneficial owners are known.</p>
Nature of Finance Function	<p>The entity has a centralizedcentralised finance function, including centralizedcentralised activities related to financial reporting.</p> <p>There are few employees involved in financial reporting roles (e.g., 5 individuals or less).</p>
Information Technology (IT)	<p>The IT environment of the entity, including its IT applications and IT processes, is straightforward.</p> <p>The entity uses commercial software and does not have the ability to make any programme changes other than to configure the software (e.g., the chart of accounts, reporting parameters or thresholds).</p> <p>Access to the software is generally limited to one or two designated individuals for the purpose of making the configurations.</p> <p>Few formalizedformalised general IT controls are needed in the entity's circumstances.</p>
Application of the Financial Reporting Framework and Accounting Estimates	<p>Few accounts or disclosures in the financial statements of the entity necessitate the use of significant management judgmentjudgement in applying the requirements of the financial reporting framework.</p> <p>The entity's financial statements ordinarily do not include accounting estimates that involve the use of methods, models, assumptions, or data, that are complex.</p>

Additional Characteristics Relevant for Group Audits	
For group audits, the following qualitative characteristics are to be considered in addition to those above:	
Group Structure and Activities	The group has few entities or business units (e.g., 5 or less). Entities or business units within the group operate in jurisdictions with similar characteristics, for example laws or regulations and business practices.
Access to Information or People	Group management will be able to provide the engagement team with access to information and unrestricted access to persons within the group as determined necessary by the group auditor.
Consolidation Process	The group has a simple consolidation process. For example: <ul style="list-style-type: none"> • Intercompany or other consolidation adjustments are not complex; • Financial information of all entities or business units has been prepared in accordance with similar accounting policies applied to the group financial statements; and • All entities or business units have the same financial reporting period-end as that used for group financial reporting.

Notwithstanding that professional ~~judgment~~judgement is applied in determining whether this standard is appropriate to use, if there is uncertainty about whether an audit meets the criteria as set out in this Authority, the use of the ~~ISA for LCE~~ISA (NZ) for LCE is not appropriate.

Quantitative Thresholds

A.4. ~~[Amended by the NZAuASB]~~

~~NZA.4. [Section deleted by the NZAuASB – no quantitative thresholds are applicable under the ISA (NZ) for LCE] Determining quantitative thresholds assists in the consistent and appropriate use of the ISA for LCE in a jurisdiction. This section anticipates that legislative or regulatory authorities or relevant local bodies with standard setting authority will determine quantitative threshold(s) for use of the ISA for LCE in their respective jurisdictions.~~

~~Guidance on setting quantitative thresholds is described further in the Authority Supplemental Guide. Quantitative thresholds may be set, for example, for all applicable entities within the jurisdiction in general, or different thresholds may be set for entities within specific or certain industries or for certain classes of entities. In doing so, consideration is to be given to the specific prohibitions for use of the ISA for LCE and the qualitative characteristics of an LCE, as set out in this Part, as well as other specific circumstances or needs that may be relevant in the jurisdiction. While complexity is not always directly relative to the size of an entity or its activities, complexity often increases when key quantitative measures (e.g., revenue, total assets, employee numbers etc.,) increase.~~

~~When determining quantitative thresholds for the use of the ISA for LCE, existing definitions or thresholds in a jurisdiction, developed for different purposes, may be considered for example:~~

~~• European Commission's definition of a "small enterprise."⁶ A small enterprise is defined as an enterprise which employs fewer than 50 persons and whose annual turnover or annual balance sheet total does not exceed EUR 10 million.~~

~~• The South African Department of Small Business Development's definition of "small enterprise."⁷ This definition includes the size category, 'small', which is an enterprise with 50 or fewer full-time equivalent paid employees and a total annual turnover not exceeding a specific threshold depending on the enterprise's sector or subsector of the economy.~~

~~The IAASB considered that these definitions or thresholds may be appropriate examples for a jurisdiction to consider when determining quantitative thresholds, adjusted for the economic and other circumstances of the jurisdiction.~~

~~When the auditor is determining whether the ISA for LCE is appropriate to use, quantitative thresholds established in a jurisdiction are to be considered in addition to the specific prohibitions in paragraph A.1. and the qualitative characteristics in paragraph A.3.~~

Responsibilities of Legislative or Regulatory Authorities or Relevant Local Bodies

NZA.5. The XRB permits the voluntary application of the ISA (NZ) for LCE in specific circumstances.

Auditors may voluntarily adopt this standard:

(a) On or after the mandatory date, or early adoption accounting period, as defined in the Commencement and Application section of this standard; and

(b) The auditor determines that the audit engagement can be undertaken using the ISA (NZ) for LCE in accordance with Part A of this standard. (Ref: Para. 3.2.9., 4.3.1., 6.5.1., 8.5.1.).

Decisions about the required or permitted use of the IAASB's International Standards (including the International Standards on Auditing and the ISA for LCE) rest with legislative or regulatory authorities or relevant local bodies with standard-setting authority (such as regulators or oversight bodies, jurisdictional / national auditing standard setters, professional accountancy organizations or others as appropriate) in individual jurisdictions.

As part of the local adoption and implementation process, it is anticipated that legislative or regulatory authorities or relevant local bodies with standard-setting authority:

- May add or modify the classes of entities in paragraph A.1.(c) as set out in paragraph A.2.*
- Determine quantitative thresholds described in paragraph A.4. (Not applicable for NZ)*

In doing so, the specific prohibitions and qualitative characteristics should be considered, as well as other specific needs that may be relevant in the jurisdiction.

1. Fundamental Concepts, General Principles and Overarching Requirements

Content of this Part

Part 1 sets out the:

- ~~Effective date of this standard.~~
- The relevant ethical requirements and obligations for firm-level quality management.
- Overall objectives of the auditor. Each Part within this standard contains an objective for planning and performing the audit, and provides a link between the requirements within that Part and the overall objectives of the auditor. The objectives within each Part assist the auditor to understand the intended outcomes of the procedures contained in that Part.
- Fundamental concepts, general principles, and overarching requirements applicable to the engagement, including professional ~~judgment~~judgement and professional ~~skepticism~~scepticism.
- Overarching requirements in relation to fraud, law or regulation, related parties, and communications with management and, where appropriate, those charged with governance.
- General communication requirements that apply to all Parts. Within individual Parts there may be additional specific communication requirements.

Scope of this Part

The concepts, principles and overarching requirements in this Part apply throughout the audit engagement.

1.1. Effective Date

1.1.1. ~~This standard is effective for audits of financial statements of LCEs for periods beginning on or after December 15, 2025. [Deleted by NZAuASB, refer to Commencement and Application section on page xx]~~

1.2. Relevant Ethical Requirements and Firm-Level Quality Management

Relevant Ethical Requirements for an Audit of Financial Statements

1.2.1. The auditor shall comply with relevant ethical requirements, including those pertaining to independence, for financial statement audit engagements.

~~[NZ] Relevant ethical requirements in New Zealand ordinarily comprise the provisions of Professional and Ethical Standard 1, the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Assurance Practitioners Accountants (including International Independence Standards) (IESBA New Zealand Code) related to an audit of financial statements, together with national requirements that are more restrictive.~~

~~The IESBA Code Professional and Ethical Standard 1 (PES 1) establishes the fundamental principles of ethics, which are:~~

- Integrity;
- Objectivity;
- Professional competence and due care;

- Confidentiality; and
- Professional ~~behavior~~behaviour.

The fundamental principles of ethics establish the standard of ~~behavior~~behaviour expected of an ~~assurance practitioner~~professional accountant. The ~~IESBA Code~~PES 1 provides a conceptual framework that establishes the approach which an ~~assurance practitioner~~professional accountant is required to apply when identifying, evaluating and addressing threats to compliance with the fundamental principles.

Firm-Level Quality Management

1.2.2. [Amended by the NZAuASB]

NZ1.2.2. The engagement partner shall be a member of a firm that applies PES 3⁸ and PES 4⁹the ISQMs, or national requirements that are at least as demanding as PES 3 and PES 4the ISQMs.

[NZ] Systems of quality management, including the policies or procedures, are the responsibility of the firm. ~~ISQM 1~~PES 3, applies to all firms that perform ~~audits~~engagements governed by the Standards of the External Reporting Board (XRB). If an engagement quality review is required by the firm's policies or procedures established in accordance with ~~ISQM 1~~PES 3, then ~~ISQM 2~~,¹⁰PES 4 applies. ~~ISQM 2~~PES 4 deals with the appointment and eligibility of the engagement quality reviewer, and the performance and documentation of the engagement quality review.

1.3. Overall Objectives of the Auditor

1.3.1. The overall objectives of the auditor when conducting an audit of financial statements using the ~~ISA for LCE~~ISA (NZ) for LCE are to:

- Obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, to enable the auditor to express an opinion on whether the financial statements are prepared, in all material respects in accordance with an applicable financial reporting framework; and
- Report on the financial statements, and communicate as required by this standard, in accordance with the auditor's findings.

1.3.2. The auditor shall obtain an understanding of the entire text of this standard to understand its objectives and to apply its requirements properly.

1.3.3. To achieve the overall objectives, the auditor shall use the objectives stated in the relevant Parts in planning and performing the audit, to:

- Determine whether any audit procedures in addition to those required by the relevant Part are necessary to achieve the objectives stated in this standard; and
- Evaluate whether sufficient appropriate audit evidence has been obtained.

The auditor is required to use the objectives to evaluate whether sufficient appropriate audit evidence has been obtained in the context of the overall objectives of the auditor. If as a result the auditor concludes that the audit evidence is not sufficient and appropriate, then the auditor may follow one or more of the following approaches:

⁸ Professional and Ethical Standard (PES) 3 *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

⁹ Professional and Ethical Standard (PES) 4 *Engagement Quality Reviews*

- Evaluate whether further relevant audit evidence has been, or will be, obtained as a result of complying with requirements from other Parts;
- Extend the work performed in applying one or more requirements; or
- Perform other procedures judged by the auditor to be necessary in the circumstances.

1.3.4. If an objective in a Part cannot be achieved, the auditor shall evaluate whether this prevents the auditor from achieving the overall objectives of the auditor and thereby requires the auditor to:

- Modify the terms of engagement and perform the audit and report in accordance with the International Standards on Auditing (New Zealand); or
- Modify the auditor's opinion or withdraw from the engagement (where withdrawal is possible under applicable law or regulation).

Failure to achieve an objective represents a significant matter requiring documentation.

1.4. Fundamental Concepts and General Principles for Performing the Audit

1.4.1. The auditor shall comply with all relevant requirements unless, in exceptional circumstances, the auditor judges it necessary to depart from a relevant requirement. In such circumstances the auditor shall perform alternative procedures to achieve the aim of that requirement. The need for the auditor to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the aim of the requirement.

[NZ] A requirement is not relevant only in the cases where the entire Part is not relevant (for example, if the audit is not a group audit, or if the audit does not include the audit of service performance information; or the requirement is conditional and the condition does not exist (for example, the requirement to modify the auditor's opinion where there is an inability to obtain sufficient appropriate audit evidence, and there is no such inability).

1.4.2. The auditor shall not represent compliance with the ~~ISA for LCE~~ ISA (NZ) for LCE in the auditor's report unless all relevant requirements in this standard have been met or the circumstances in paragraph 1.4.1. apply.

Professional ~~Judgment~~ Judgement

1.4.3. The auditor shall exercise professional ~~judgment~~ judgement in planning and performing the audit.

Professional ~~judgment~~ judgement is essential to the proper conduct of an audit. This is because interpretation of relevant ethical requirements and this standard and the informed decisions required throughout the audit cannot be made without the application of relevant knowledge and experience to the facts and circumstances.

The distinguishing feature of the professional ~~judgment~~ judgement expected of an auditor is that it is exercised by an auditor whose training, knowledge and experience have been sufficiently developed to achieve the necessary competencies for reasonable ~~judgment~~ judgements.

The exercise of professional ~~judgment~~ judgement in any particular case is based on the facts and circumstances that are known to the auditor.

Significant professional ~~judgment~~ judgements made in reaching conclusions on significant matters arising during the audit are required to be documented in accordance with the requirements of Part 2 of this standard.

Professional ~~Skepticism~~Scepticism

1.4.4. The auditor shall plan and perform the audit with professional ~~skepticisms~~scepticism ~~recognizing~~recognising that circumstances may exist that cause the financial statements to be materially misstated.

1.4.5. The auditor shall design and perform procedures in a way that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory.

Professional ~~skepticisms~~scepticism includes being alert to, for example:

- *Audit evidence that contradicts other audit evidence obtained.*
- *Information that brings into question the reliability of documents and responses to ~~e~~inquiries to be used as audit evidence.*
- *Conditions that may indicate possible fraud.*
- *Circumstances that suggest the need for audit procedures in addition to those required by this standard.*

Professional ~~skepticisms~~scepticism is necessary to the critical assessment of audit evidence. This includes questioning contradictory audit evidence and the reliability of documents and responses to ~~e~~inquiries and other information obtained from management, and where appropriate, those charged with governance. It also includes consideration of the sufficiency and appropriateness of audit evidence obtained in the light of the circumstances.

The auditor cannot be expected to disregard past experience of the honesty and integrity of the entity's management, and where appropriate, those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the auditor of the need to maintain professional ~~skepticisms~~scepticism or allow the auditor to be satisfied with less than persuasive audit evidence when obtaining reasonable assurance.

Conditions of the engagement can create pressures on the engagement team that may impede the appropriate exercise of professional ~~skepticisms~~scepticism when designing and performing audit procedures and when evaluating audit evidence.

1.5. Fraud

The primary responsibility for the prevention and detection of fraud rests with both management, and where appropriate, those charged with governance of the entity. Although fraud is a broad legal concept, for the purposes of this standard, the auditor is concerned with fraud that causes a material misstatement in the financial statements.

Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional. Two types of intentional misstatements are relevant to the auditor – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets. Although the auditor may suspect or, in rare cases, identify the occurrence of fraud, the auditor does not make legal determinations of whether fraud has actually occurred.

An auditor conducting an audit in accordance with this standard is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error even though

the audit is properly planned and performed in accordance with this standard. This is because fraud may involve sophisticated and carefully ~~organized~~organised schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor.

When obtaining reasonable assurance, the auditor is responsible for:

- *Maintaining professional ~~skepticism~~scepticism throughout the audit;*
- *Considering the potential for management override of controls; and*
- *~~Recognizing~~Recognising the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud.*

1.5.1. The auditor shall address the risk of fraud when:

- (a) Identifying and assessing risks of material misstatement, whether due to fraud or error. In doing so, the auditor shall 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;¹¹
- (b) Obtaining sufficient appropriate audit evidence through designing and implementing appropriate responses to assessed risks of material misstatement, including risks of material misstatement due to fraud; and
- (c) Responding appropriately to fraud or suspected fraud identified during the audit.

Considerations Specific to Public Sector Entities

The public sector auditor's responsibilities relating to fraud may be a result of law, regulation or other authority applicable to public sector entities or separately covered by the auditor's mandate. Consequently, the public sector auditor's responsibilities may not be limited to consideration of risks of material misstatement of the financial statements, but may also include a broader responsibility to consider risks of fraud.

Auditor Unable to Continue the Engagement

1.5.2. If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor shall determine the legal and professional responsibilities applicable in the circumstances or consider whether it is appropriate to withdraw, where withdrawal is possible under law or regulation.

Considerations Specific to Public Sector Entities

In many cases in the public sector, the option of withdrawing from the engagement may not be available to the auditor due to the nature of the mandate or public interest considerations.

1.6. Laws and Regulations

It is the responsibility of management, with the oversight of those charged with governance where appropriate, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements.

¹¹ Appendix 4 sets out fraud risk factors relevant to less complex entities.

The requirements in this standard are designed to assist the auditor in identifying material misstatement of the financial statements due to non-compliance with laws and regulations. However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations. The auditor's focus in an audit of the financial statements is on circumstances when non-compliance with laws or regulations results in a material misstatement of the financial statements. In this regard, the auditor's responsibilities are in relation to compliance with two different categories of laws and regulations and are distinguished as follows:

- *The provisions of those laws and regulations generally ~~recognized~~recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements (e.g., tax and pension laws and regulations); and*
- *Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (e.g., compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations), i.e., non-compliance with such laws and regulations may therefore have a material effect on the financial statements.*

- 1.6.1. During the audit, the auditor shall remain alert to the possibility that performing audit procedures may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention.

In the absence of identified or suspected non-compliance, the auditor is not required to perform audit procedures regarding the entity's compliance with laws and regulations, other than what is required by this standard.

Considerations Specific to Public Sector Entities

In the public sector, there may be additional audit responsibilities with respect to the consideration of laws and regulations which may relate to the audit of financial statements or may extend to other aspects of the entity's operations.

Reporting to an Appropriate Authority Outside the Entity

- 1.6.2. If the auditor has identified or suspects non-compliance with laws and regulations, including fraud, the auditor shall determine whether law, regulation or relevant ethical requirements:

- (a) Require the auditor to report to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

Reporting identified or suspected non-compliance with laws and regulations, including fraud, to an appropriate authority outside the entity may be required or appropriate in the circumstances because:

- *The auditor has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements; or*
- *Law, regulation or relevant ethical requirements provide the auditor with the right to do so.*

1.7. Related Parties

1.7.1. During the audit, the auditor shall remain alert for:

- (a) Information about the entity's related parties, including circumstances involving a related party with dominant influence;
- (b) Arrangements or other information that may indicate the existence of related party relationships or transactions that management has not previously identified or disclosed to the auditor; and
- (c) Significant transactions outside the entity's normal course of business.

Many related party transactions occur in the normal course of business. In such circumstances, they may carry no higher risk of material misstatement of the financial statements than similar transactions with unrelated parties. However, the nature of related party relationships and transactions may, in some circumstances, give rise to higher risks of material misstatement of the financial statements than transactions with unrelated parties. Related parties, by virtue of their ability to exert control or significant influence, may be in a position to exert dominant influence over the entity or its management. Consideration of such ~~behavior~~behaviour is relevant when identifying and assessing the risks of material misstatement due to fraud.

Many financial reporting frameworks establish specific accounting and disclosure requirements for related party relationships, transactions and balances to enable users of the financial statements to understand their nature and actual or potential effects on the financial statements. Where the financial reporting framework has established such requirements, the auditor has a responsibility to perform audit procedures to identify, assess and respond to the risks of material misstatement arising from the entity's failure to appropriately account for or disclose related party relationships, transactions or balances in accordance with the requirements of the framework. Even if the applicable financial reporting framework has not established such requirements, the auditor nevertheless needs to obtain an understanding of the entity's related party relationships and transactions to be able to conclude whether the financial statements achieve fair presentation for fair presentation frameworks or are not misleading for compliance frameworks.

1.8. General Communications with Management and Those Charged with Governance

1.8.1. The auditor shall determine the appropriate person(s) within the entity's governance structure with whom to communicate.

1.8.2. The auditor shall communicate with those charged with governance the relevant ethical requirements, including those related to independence, that the auditor applies for the audit engagement.

1.8.3. The auditor shall communicate, on a timely basis, with management and, where appropriate, those charged with governance.

Governance structures vary by jurisdiction and by entity, reflecting influences such as different cultural and legal backgrounds, and size and ownership characteristics. Governance is the collective responsibility of a governing body, such as a board of directors, a supervisory board, partners, proprietors, a committee of management, a council of governors, trustees or equivalent.

There may be other cases where it is not clear with whom to communicate, for example in some family-owned businesses, some not-for-profit organizations and some government entities (e.g., the governance structure may not be defined). In such cases the auditor may need to discuss and agree with management or the engaging party with whom communications should be made.

1.8.4. Specific matters to be communicated are required throughout this standard. The auditor shall use professional ~~judgment~~judgement in determining the appropriate form, timing, and general content

of the communications with management, and where appropriate, those charged with governance. When determining the form and timing of communication, the auditor shall consider:

- (a) Legal requirements for communication; and
- (b) The significance of the matters to be communicated.

The appropriate form and timing of communications will vary with the circumstances of the audit, and may be affected by the significance and nature of the matter, and the actions expected to be taken by management, and where appropriate, those charged with governance.

Communication with management and, where appropriate, those charged with governance, often may occur in a less structured manner and matters may be communicated orally. This standard requires that the auditor exercises professional judgement to determine when oral communication of a matter would not be adequate and communication in writing is appropriate. In addition, certain matters are required to be communicated in writing, as set out in this standard.

- 1.8.5. In some cases, all of those charged with governance are involved in managing the entity, for example, an LCE where a single owner manages the entity and no one else has a governance role. In these cases, if matters required by this standard are communicated with person(s) with management responsibilities, and those person(s) also have governance responsibilities, the matters need not be communicated again with those same person(s) in their governance role. The auditor shall nonetheless be satisfied that communication with person(s) with management responsibilities adequately informs all of those with whom the auditor would otherwise communicate in their governance capacity.
- 1.8.6. Where the responses to inquiries of management, and where appropriate, those charged with governance about a particular matter are inconsistent, the auditor shall investigate the inconsistency.

Specific Communications in Relation to Fraud

- 1.8.7. If the auditor has identified fraud or has obtained information that indicates that fraud may exist, the auditor shall communicate these matters, unless prohibited by law or regulation, on a timely basis to the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities.

Considerations Specific to Public Sector Entities

In the public sector, requirements for reporting fraud, whether or not discovered through the audit process, may be subject to specific provisions of the audit mandate or related law, regulation or other authority.

- 1.8.8. Unless prohibited by law or regulation, the auditor shall communicate with those charged with governance, on a timely basis, if the auditor has identified or suspects fraud involving:
- (a) Management, unless those charged with governance are involved in managing the entity;
 - (b) Employees who have significant roles in the entity's system of internal control; or
 - (c) Others where the fraud results in a material misstatement in the financial statements.
- 1.8.9. If the auditor suspects fraud involving management, the auditor shall discuss with those charged with governance the nature, timing and extent of audit procedures necessary to complete the audit.

1.9. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

- 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

Content of this Part

Part 2 sets out the requirements to be applied throughout the audit for:

- Audit evidence.
- Documentation. Within individual Parts there may also be additional specific documentation requirements.

Scope of this Part

The requirements in this Part apply throughout the audit engagement.

2.1. Objectives

2.1.1. The objectives of the auditor are to:

- (a) Design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion; and
- (b) Prepare documentation that provides a sufficient and appropriate record of the basis for the auditor's report and provides evidence that the audit was planned and performed in accordance with the ~~ISA for LCE~~ ISA (NZ) for LCE and applicable law or regulation.

2.2. Sufficient Appropriate Audit Evidence

2.2.1. To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level thereby enabling the auditor to draw reasonable conclusions on which to base the auditor's opinion.

2.2.2. The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.

Sufficiency is the measure of the quantity of audit evidence. It is affected by the auditor's assessment of the risks of material misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also the quality of the audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate if it is of poor quality.

Appropriateness is the measure of the quality of the audit evidence, that is its relevance and reliability in providing support for the conclusions on which the auditor's opinion is based.

Most of the auditor's work in forming the auditor's opinion consists of obtaining and evaluating audit evidence. Whether sufficient appropriate audit evidence has been obtained to reduce audit risk to an acceptably low level, and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion, is a matter of professional ~~judgment~~ judgement.

2.3. Information to be Used as Audit Evidence

Audit evidence to draw reasonable conclusions on which to base the auditor's opinion is obtained by designing and performing procedures to identify and assess risks of material misstatement (see

Part 6) and responding to assessed risks of material misstatement (see Part 7), as well as procedures in other Parts to comply with the requirements of the ~~ISA for LCE~~ ISA (NZ) for LCE.

Audit procedures to obtain audit evidence can include inspection, observation, confirmation, recalculation, reperformance and analytical procedures, often in some combination, in addition to einquiry. Although einquiry may provide important audit evidence, and may even produce evidence of a misstatement, einquiry alone ordinarily does not provide sufficient audit evidence of the absence of a material misstatement at the assertion level, nor of the operating effectiveness of controls.

Audit evidence is cumulative in nature and is primarily obtained from audit procedures performed during the audit, but may also include information from other sources, such as:

- Previous audits (provided that the auditor has confirmed there are no changes);
- Other engagements performed for the client; and
- The firm's quality management procedures for acceptance and continuance.

Audit evidence may come from inside or outside the entity (the entity's accounting records are an important source of audit evidence), the work of management's expert, and includes information that both supports and corroborates management's assertions, as well as contradicts such assertions.

Automated Tools and Techniques (ATT)

ATT, for the purpose of this standard, are IT-enabled processes that involve the automation of methods and procedures, for example the analysis of data using modelling and visualization, or drone technology to observe or inspect assets.

In applying this standard, an auditor may design and perform audit procedures manually or through the use of ATT, and either technique can be effective. Regardless of the tools and techniques used, the auditor is required to comply with the requirements in this standard.

Using ATT can supplement or replace manual or repetitive tasks. In certain circumstances, when obtaining audit evidence, an auditor may determine that the use of ATT to perform certain audit procedures may result in more persuasive audit evidence relative to the assertion being tested. In other circumstances, performing audit procedures may be effective without the use of ATT.

The use of ATT may potentially create biases or a general risk of overreliance on the information or output of the audit procedure performed. As powerful as these tools may be, they are not a substitute for the auditor's knowledge and professional ~~judgment~~ judgment. Further, although the auditor may have access to a wide array of data, including from varying sources (i.e., increased quantity), the exercise of professional ~~skepticism~~ skepticism remains necessary to critically assess audit evidence arising from the use of data and from the outputs from using ATT.

- 2.3.1. When designing and performing audit procedures, the auditor shall consider the relevance and reliability of the information to be used as audit evidence, including information from external information sources.

Relevance deals with the logical connection with, or bearing upon, the purpose of the audit procedure and, where appropriate, the assertion under consideration. The relevance of the information may be affected by the direction of testing.

The reliability of information to be used as audit evidence is influenced by its source and nature, as well as the circumstances under which it was obtained, including the controls over its preparation and maintenance where relevant. Generally, the reliability of information is increased when it is obtained from independent sources outside of the entity, by the auditor directly, is an original

document rather than a copy and is written rather than oral information. However, circumstances may exist that could affect these generalizations.

2.3.2. When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes including, as necessary in the circumstances:

- (a) Obtaining evidence about the accuracy and completeness of the information; and
- (b) Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes.

Obtaining audit evidence about the accuracy and completeness of such information may be performed concurrently with the actual audit procedure applied to the information when obtaining such audit evidence is an integral part of the audit procedure itself. In other situations, the auditor may have obtained audit evidence of the accuracy and completeness of such information by testing controls over the preparation and maintenance of the information. In some situations, however, the auditor may determine that additional audit procedures are needed.

2.3.3. Unless the auditor has reason to believe the contrary, the auditor may accept records and documents as genuine. If conditions identified during the audit cause the auditor to believe that a document may not be authentic or that terms in a document have been modified but not disclosed to the auditor, the auditor shall investigate further and determine the effect on the rest of the audit evidence obtained.

2.3.4. The auditor shall determine what modifications or additions to audit procedures are necessary if:

- (a) Audit evidence obtained from one source is inconsistent with that obtained from another; or
- (b) The auditor has doubts about the reliability of information to be used as audit evidence.

2.4. General Documentation Requirements

The ~~ISA for LCE~~ ISA (NZ) for LCE sets out general documentation requirements in this Part and, as appropriate, specific documentation requirements in other Parts. A documentation requirement applies only to requirements that are relevant in the circumstances.

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 ~~judgment~~ judgements made in reaching those conclusions.

Audit documentation provides evidence that the audit complies with the ~~ISA for LCE~~ ISA (NZ) for LCE. The form, content and extent of audit documentation depends on the nature and circumstances of the entity and the procedures being performed.

Audit documentation may be in paper or electronic format. Oral explanations, by the auditor on their own, do not adequately support the work performed by the auditor or the conclusions reached, but may be used to explain or clarify information contained in the audit documentation.

It is not necessary to include superseded drafts of working papers or financial statements in the audit documentation.

It is not necessary or practicable for the auditor to document every matter considered, or professional ~~judgment~~judgement made, in an audit. However, the auditor is required to prepare audit documentation that provides a sufficient and appropriate record of the basis for the auditor's report and provides evidence that the audit was planned and performed in accordance with the ~~ISA for LCE~~ISA (NZ) for LCE and applicable law or regulation. Further, it is unnecessary for the auditor to document separately (as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file.

Significant Matters

Judging the significance of a matter requires professional ~~judgment~~judgement and the analysis of the facts and circumstances. Examples of significant matters include matters giving rise to significant risks, areas where the financial statements could be materially misstated, circumstances where the auditor has had difficulty in applying the necessary audit procedures, or any findings that could result in a modified opinion.

When the Engagement Partner Performs All the Audit Work

In the case of an audit where the engagement partner performs all the audit work, the documentation will not include matters that might have to be documented solely to inform or instruct members of an engagement team, or to provide evidence of review by other members of the team (e.g., there will be no matters to document relating to team discussions or supervision). Nevertheless, the engagement partner complies with the overriding requirement to prepare audit documentation that can be understood by an experienced auditor, as the audit documentation may be subject to review by external parties for regulatory or other purposes.

Automated Tools and Techniques

This standard does not differentiate between different tools and techniques that the auditor may use to design and perform audit procedures, for example using manual or automated techniques with respect to what is required to be documented. Regardless of the tools and techniques used, the auditor is required to comply with relevant documentation requirements.

- 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

Content of this Part

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

Scope of this Part

In accordance with ~~ISQM 4~~**PES 3**, the firm is responsible for designing, implementing, and operating a system of quality management for audits of financial statements, that provides the firm with reasonable assurance that:

- The firm and its personnel ~~fulfill~~**fulfil** their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and
- Engagement reports issued are appropriate in the circumstances.

The engagement team, led by the engagement partner, is responsible within the context of the firm's system of quality management for:

- Implementing the firm's responses to quality risks that are applicable to the audit engagement using information communicated by, or obtained from, the firm;
- Determining whether additional responses are needed at the engagement level beyond those in the firm's policies or procedures given the nature and circumstances of the engagement; and
- Communicating to the firm information from the audit engagement that is required to be communicated by the firm's policies or procedures to support the design, implementation, and operation of the firm's system of quality management.

The requirements in this Part apply throughout the audit engagement.

3.1. Objective

3.1.1. The objective of the auditor is to manage quality at the engagement level to obtain reasonable assurance that quality has been achieved such that:

- (a) The auditor has fulfilled the auditor's responsibilities, and has conducted the audit, in accordance with this standard and applicable legal and regulatory requirements; and
- (b) The auditor's report issued is appropriate in the circumstances.

3.2. The Engagement Partner's Responsibilities

Leadership Responsibilities for Managing and Achieving Quality

3.2.1. The engagement partner shall take:

- (a) Overall responsibility for managing and achieving quality on the audit engagement, including being sufficiently and appropriately involved throughout the audit engagement such that the engagement partner has the basis for determining whether the significant ~~judgment~~**judgements** made, and conclusions reached are appropriate in the circumstances; and
- (b) Responsibility for clear, consistent and effective actions being taken that reflect the firm's commitment to quality.

The engagement partner's responsibility for managing and achieving quality is supported by a firm culture that demonstrates a commitment to quality.

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

3.2.2. In taking overall responsibility for managing and achieving quality on the audit engagement, the engagement partner shall determine that the nature, timing and extent of direction, supervision and review is:

- (a) Responsive to the nature and circumstances of the engagement and the resources assigned; and
- (b) Planned and performed in accordance with the firm's policies or procedures, this standard, relevant ethical requirements and regulatory requirements.

Sufficient and Appropriate Involvement

Being sufficiently and appropriately involved throughout the audit engagement when procedures, tasks or actions have been assigned to other members of the engagement team may be demonstrated by the engagement partner in different ways, including:

- *Informing assignees about the nature of their responsibilities and authority, the scope of the work being assigned and the objectives thereof; and to provide any other necessary instructions and relevant information.*
- *Direction and supervision of the assignees.*
- *Review of the assignees' work to evaluate the conclusions reached.*

Direction, Supervision and Review

The approach to direction, supervision and review may be tailored depending on, for example:

- *The engagement team member's previous experience with the entity and the area to be audited.*
- *The assessed risks of material misstatement. A higher assessed risk of material misstatement may require a corresponding increase in the extent and frequency of the direction and supervision of engagement team members and a more detailed review of their work.*
- *The competence and capabilities of the individual engagement team members performing the audit work.*

3.2.3. The engagement partner shall take responsibility for establishing and communicating to the members of the engagement team the expected ~~behavior~~behaviour of the engagement team members, including ~~emphasizing~~emphasising:

- (a) That all engagement team members are responsible for contributing to the management and achievement of quality at the engagement level;
- (b) The importance of professional ethics, values and attitudes;
- (c) The importance of open and robust communication within the engagement team, and supporting the ability of engagement team members to raise concerns without fear of reprisal; and

- (d) The importance of exercising professional ~~skepticism~~scepticism throughout the audit engagement.

In addressing the requirements in paragraphs 3.2.2. and 3.2.3., the engagement partner may communicate directly to other members of the engagement team and reinforce this communication through conduct and actions (e.g., leading by example).

Relevant Ethical Requirements

3.2.4. The engagement partner shall have an understanding of the relevant ethical requirements, including those related to independence, that are applicable given the nature and circumstances of the audit engagement.

3.2.5. If matters come to the engagement partner's attention that indicate that a threat to compliance with relevant ethical requirements exists or relevant ethical requirements have been breached, the engagement partner shall take action, including:

- (a) Following the firm's policies or procedures to evaluate the threat; and
- (b) Consulting with others in the firm.

If there are no others in the firm to consult with, the engagement partner may consult with others outside the firm such as experienced practitioners in other firms or the professional accountancy body where the engagement partner is a member.

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

3.2.6. Throughout the audit engagement, the engagement partner shall:

- (a) Take responsibility for other members of the engagement team having been made aware of relevant ethical requirements and the firm's related policies or procedures for identifying, evaluating, and addressing threats to compliance with relevant ethical requirements; and
- (b) Remain alert, through observation and making ~~e~~inquiries as necessary, for breaches of relevant ethical requirements by members of the engagement team.

Engagement Resources

3.2.7. Taking into account the nature and circumstances of the audit and the firm's related policies or procedures, the engagement partner shall:

- (a) Determine that:
 - (i) Sufficient and appropriate resources are assigned or made available to the engagement team in a timely manner; and
 - (ii) Members of the engagement team, and any auditor's external experts, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement.
- (b) If the conditions in (a) are not met, the engagement partner shall take appropriate action.

Other Engagement Partner Responsibilities

3.2.8. The engagement partner shall:

- (a) Obtain an understanding of the information from the firm's monitoring and remediation process, as communicated by the firm, including, as applicable, the information from the monitoring and remediation process of the network and across the network firms, and:
 - (i) Determine the relevance and effect of that information on the audit engagement; and
 - (ii) Take appropriate action; and
- (b) Remain alert for matters that may be relevant to the firm's monitoring and remediation process and communicate to those responsible for the process.

3.2.9. The engagement partner shall:

- (a) Take responsibility for differences of opinion being addressed and resolved in accordance with the firm's policies or procedures;
- (b) Take responsibility for consultations being undertaken in accordance with the firm's related policies or procedures, or where deemed necessary on difficult or contentious matters;
- (c) Determine that conclusions reached with respect to differences of opinion and difficult or contentious matters are documented, agreed with the party consulted, and implemented; and
- (d) Not date the auditor's report until any differences of opinion are resolved.

Forming an objective view on the appropriateness of the ~~judgment~~ judgements made in the course of the audit can present practical problems when the same individual also performs the entire audit. If unusual issues are involved, it may be desirable to consult with other suitably experienced auditors or the professional accountancy body.

Consultation may be appropriate, or required by the firm's policies or procedures, when there are:

- *Issues that are complex or unfamiliar;*
- *Significant risks;*
- *Significant transactions that are outside the normal course of business or that otherwise appear to be unusual;*
- *Limitations imposed by management; or*
- *Non-compliance with law or regulation.*

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.

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~~ ISA (NZ) for LCE continues to be appropriate.

3.2.10. For audit engagements for which an engagement quality review is required, the engagement partner shall determine that an engagement quality reviewer has been appointed and:

- (a) Cooperate with the engagement quality reviewer;
- (b) Discuss significant matters and significant ~~judgment~~judgements arising during the audit with the engagement quality reviewer; and
- (c) Not date the auditor's report before the engagement quality review is complete.

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

3.2.11. The engagement partner shall review audit documentation at appropriate points in time during the audit, including documentation of:

- (a) Significant matters;
- (b) Significant ~~judgment~~judgements and the conclusions reached; and
- (c) Other matters that, in the engagement partner's professional ~~judgment~~judgement, are relevant to the engagement partner's responsibilities.

The engagement partner exercises professional ~~judgment~~judgement in determining matters to review, for example, based on:

- *The nature and circumstances of the audit engagement.*
- *Which engagement team member performed the work.*
- *Matters from recent inspection findings.*
- *The requirements of the firm's policies or procedures.*

3.2.12. The engagement partner shall review, prior to their issuance, formal written communications to management, those charged with governance or regulatory authorities.

3.3. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

3.3.1. The auditor shall include in the audit documentation:

- (a) Matters identified, relevant discussions, and conclusions reached with respect to ~~fulfillment~~fulfilment 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

Content of this Part

Part 4 sets out the auditor's responsibilities for:

- Agreeing the terms of the audit engagement with management, and where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit are present.
- Determining that use of the ~~ISA for LCE~~ ISA (NZ) for LCE is appropriate for the audit engagement.

Part 4 also addresses activities related to initial audit engagements.

Scope of this Part

Part A of this standard sets out the authority for determining the appropriate use of the ~~ISA for LCE~~ ISA (NZ) for LCE. This Part sets out the engagement partner's obligations for use of this standard as part of the firm's acceptance or continuance procedures for an audit engagement of an LCE.

The information and audit evidence gathered during client acceptance and continuance procedures is used to make the determination that the ~~ISA for LCE~~ ISA (NZ) for LCE is appropriate for the audit engagement, and informs the auditor's procedures when planning the audit, and for risk identification and assessment.

The Preface sets out that this standard is premised on the basis that the firm is subject to ~~ISQM 4~~ PES 3 or to national requirements that are at least as demanding. ~~ISQM 4~~ PES 3 requires the firm to establish quality objectives that address the acceptance and continuance of client relationships and specific engagements. In addition, compliance with ~~ISQM 4~~ PES 3 may require firms to have policies or procedures to address other matters of relevance to this Part.

Audit engagements may only be accepted when the auditor considers that relevant ethical requirements such as independence and professional competence and due care will be satisfied, and the preconditions for an audit are present. In addition, the auditor considers the performance of non-assurance services for the audit client and whether these services are permissible.

If the audit is an initial engagement, this Part also sets out the auditor's responsibilities relating to opening balances.

4.1. Objectives

4.1.1. The objectives of the auditor are:

- (a) To accept or continue an audit engagement only when the basis upon which it is to be performed has been agreed, through:
 - (i) Establishing whether the preconditions for an audit are present; and
 - (ii) Confirming that there is a common understanding between the auditor and management, and where appropriate, those charged with governance, of the terms of the audit engagement.
- (b) For initial audit engagements, to obtain sufficient appropriate audit evidence about whether:
 - (i) Opening balances contain misstatements that materially affect the current period's financial statements, and

- (ii) Appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

4.2. Preconditions for an Audit

4.2.1. [Amended by the NZAuASB]

NZ4.2.1.—In order to establish whether the preconditions for an audit are present, the auditor shall:

- (a) Determine whether the financial reporting framework to be applied in the preparation of the financial statements is acceptable;
- (b) Obtain the agreement of ~~management~~ those charged with governance that ~~it~~ they acknowledges and understands ~~its~~ their responsibility on behalf of the entity:
 - (i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;
 - (ii) For such controls as those charged with governance ~~management, and where appropriate management,~~ determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
 - (iii) To provide the auditor with:
 - a. Access to all information of which ~~management~~ those charged with governance, and where appropriate management, is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - b. Additional information that the auditor may request from ~~management~~ those charged with governance, and where appropriate management for the purpose of the audit; and
 - c. Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

4.2.2. [Amended by the NZ AuASB]

NZ4.2.2. If the preconditions for an audit are not present the auditor shall discuss the matter with ~~management~~ those charged with governance. Unless required by law or regulation to do so, the auditor shall not accept the proposed audit engagement:

- (a) If the auditor has determined that the financial reporting framework to be applied in the preparation of the financial statements is unacceptable; or
- (b) If the agreement of ~~management~~ those charged with governance that it acknowledges and understands its responsibility has not been obtained.

4.2.3. If management or those charged with governance impose a limitation on the scope of the auditor's work such that the auditor believes that the limitation will result in the auditor disclaiming the opinion on the financial statements, the auditor shall not accept such a limited engagement as an audit engagement, unless required by law or regulation to do so.

4.3. Considerations in Engagement Acceptance or Continuance

Performing acceptance or continuance procedures before planning commences assists the auditor in identifying and evaluating events or circumstances that may adversely affect the auditor's ability to plan and perform the current engagement.

4.3.1. The engagement partner shall determine that:

- (a) The firm's policies or procedures regarding acceptance and continuance of the audit engagement have been followed;¹² and
- (b) Conclusions reached regarding acceptance and continuance of the audit engagement are appropriate, including that the audit engagement can be undertaken using the ~~ISA for LCE~~ ISA (NZ) for LCE in accordance with Part A of this standard.

Part A sets out the matters relevant to the engagement partner for determining the appropriate use of the ~~ISA for LCE~~ ISA (NZ) for LCE, in particular in relation to the limitations for using this standard.

Information and audit evidence gathered during client acceptance and continuance procedures may be used to make the determination about use of the ~~ISA for LCE~~ ISA (NZ) for LCE. Further information may also be obtained when performing risk identification and assessment procedures that may change the engagement partner's initial determination about use of the ~~ISA for LCE~~ ISA (NZ) for LCE in accordance with this Part. Part 6 (see paragraph 6.5. 1.) requires the engagement partner to determine whether the ~~ISA for LCE~~ ISA (NZ) for LCE continues to be appropriate for the nature and circumstances of the entity being audited during the risk identification and assessment process. Consideration of further information throughout the audit may change the engagement partner's determination about the appropriateness of the use of the ~~ISA for LCE~~ ISA (NZ) for LCE.

4.3.2. In some cases, law or regulation of the relevant jurisdiction prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of this standard. In these circumstances, the auditor shall evaluate:

- (a) Whether users may misunderstand the assurance obtained from the audit of the financial statements, and, if so,
- (b) Whether additional explanation in the auditor's report can mitigate possible misunderstanding.

4.3.3. If the auditor concludes that additional explanation in the auditor's report cannot mitigate possible misunderstanding, the auditor shall not accept the audit engagement, unless required by law or regulation to do so. An audit conducted in accordance with such law or regulation does not comply with the ~~ISA for LCE~~ ISA (NZ) for LCE. Accordingly, the auditor shall not include any reference within the auditor's report to the audit having been conducted in accordance with this ~~ISA for LCE~~ ISA (NZ) for LCE.

NZ4.3.4. Professional and Ethical Standard 1¹³, requires assurance practitioners to comply with Auditing Standards; therefore, auditors shall not sign an audit report that does not conform to the requirements of this ISA (NZ) for LCE. In the extremely rare situation described in paragraph

¹² [NZ] PES 3, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*, paragraph 30 sets out the firm's responsibilities for establishing quality objectives for the acceptance of specific engagements, including judgements relating to financial and operating priorities of the firm when deciding to accept or continue specific engagements.

¹³ Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand)

4.3.2., the auditor shall attach a separate report that conforms to the requirements of this ISA (NZ) for LCE.

4.4. Terms of the Audit Engagement

4.4.1. [Amended by the NZAuASB]

NZ4.4.1. The auditor shall agree the terms of the audit engagement with ~~management, or where appropriate,~~ those charged with governance.

[NZ] If law or regulation prescribes the responsibilities of ~~management~~ those charged with governance that are equivalent in effect to what this standard requires, the auditor may use the wording of the law or regulation to describe them in the written agreement.

Appendix 2 sets out an illustrative engagement letter.

4.4.2. On recurring audits, the auditor shall assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement.

4.4.3. The auditor shall not agree to a change in the terms of the audit engagement where there is no reasonable justification for doing so.

4.4.4. If, prior to completing the audit engagement, the auditor is requested to change the audit engagement to an engagement that conveys a lower level of assurance, the auditor shall determine whether there is reasonable justification for doing so.

Before agreeing to change an audit engagement to a review or a related service, the auditor may need to assess any legal or contractual implications of the change.

4.4.5. [Amended by the NZAuASB]

NZ4.4.5. If the terms of the audit engagement are changed, the auditor and ~~management~~ those charged with governance shall agree on and record the new terms of the engagement in an engagement letter or other suitable form of written agreement.

4.4.6. [Amended by the NZAuASB]

NZ4.4.6. If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management or those charged with governance to continue the original audit engagement, the auditor shall:

- (a) Withdraw from the audit engagement, where possible under applicable law or regulation; and
- (b) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners, or regulators.

4.5. Initial Audit Engagements

4.5.1. If the engagement is an initial audit and there has been a change in auditor, the auditor shall communicate with the predecessor auditor, in compliance with relevant ethical requirements.

4.5.2. The auditor shall read the most recent financial statements, if any, and the auditor's report thereon, if any, for information relevant to opening balances, including disclosures.

4.5.3. If the prior period's financial statements were audited by a predecessor auditor and there was a modification to the opinion, the auditor shall evaluate the effect of the matter giving rise to the

modification in assessing the risks of material misstatement in the current period's financial statements.¹⁴

4.5.4. The auditor shall obtain sufficient appropriate audit evidence¹⁵ about whether the opening balances contain misstatements that materially affect the current period's financial statements by:

- (a) Determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, have been restated;
- (b) Determining whether the opening balances reflect the application of appropriate accounting policies; and
- (c) Performing one or more of the following:
 - (i) Where the prior year financial statements were audited, inspecting the predecessor auditor's working papers to obtain evidence regarding the opening balances;
 - (ii) Evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
 - (iii) Performing specific audit procedures to obtain evidence regarding the opening balances.

The nature and extent of audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances depend on such matters as:

- *The accounting policies followed by the entity.*
- *The nature of the account balances, classes of transactions and disclosures and the risks of material misstatement in the current period's financial statements.*
- *The significance of the opening balances relative to the current period's financial statements.*
- *Whether the prior period's financial statements were audited and, if so, whether the predecessor auditor's opinion was modified.*

4.5.5. If the auditor obtains audit evidence that the opening balances contain misstatements that could materially affect the current period's financial statements, the auditor shall perform such additional audit procedures as are appropriate in the circumstances to determine the effect on the current period's financial statements.¹⁶

4.5.6 The auditor shall obtain sufficient appropriate audit evidence about whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, and whether any changes in accounting policies have been appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.¹⁷

4.6. Specific Communication Requirements

4.6.1. The auditor shall communicate with those charged with governance:

¹⁴ For the effect on the auditor's report see Part 9, paragraph 9.5.9.

¹⁵ For the effect on the auditor's report see Part 9, paragraph 9.5.6.

¹⁶ For the effect on the auditor's report see Part 9, paragraph 9.5.7.

¹⁷ For the effect on the auditor's report see Part 9, paragraph 9.5.8.

- (a) The auditor's responsibilities for forming and expressing an opinion on the financial statements prepared by management; and
- (b) That the auditor's responsibilities do not relieve management or those charged with governance of their responsibilities for oversight of the preparation of the financial statements.

4.7. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

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~~ ISA (NZ) for LCE.

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

4.7.4 [Amended by the NZ-AuASB]

NZ4.7.4. —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~~ ISA (NZ) for LCE;
- (b) The objective and scope of the audit of the financial statements;
- (c) The respective responsibilities of the auditor and ~~management~~ those charged with governance;
- (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 [Amended by the NZ-AuASB]

NZ4.7.5 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~~ those charged with governance acknowledges and understands its responsibilities.

5. Planning

Content of this Part

Part 5 sets out the auditor's responsibility to plan the audit (including holding an engagement team discussion), and the concept of materiality when planning and performing the audit.

Scope of this Part

Planning is not a discrete phase of the audit, but rather a continuous and iterative process that is updated and modified, as necessary, throughout the audit. Part 6, identifying and assessing risks of material misstatement, and Part 7, responding to assessed risks of material misstatement, are also relevant to this Part.

Some requirements within this Part are linked to procedures in other Parts and may require the auditor to perform those procedures in order to meet the requirements in this Part.

5.1. Objectives

5.1.1. The objectives of the auditor are to:

- (a) Plan the audit so that it will be performed in an effective manner; and
- (b) Apply the concept of materiality appropriately in planning and performing the audit.

5.2. Planning Activities

The nature, timing and extent of planning activities will vary according to the nature and circumstances of the entity, the size and nature of the engagement team, the engagement team members' previous experience with the entity and any changes in circumstances that occur during the audit engagement.

The purpose and objective of planning the audit are the same whether the audit is an initial or recurring engagement. However, for an initial audit, the auditor may need to expand the planning activities because the auditor does not ordinarily have the previous experience with the entity that is considered when planning recurring engagements.

5.2.1. The auditor shall set the scope, timing and direction of the audit and:

- (a) Identify the characteristics of the engagement that define its scope;
- (b) Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required;
- (c) Consider the factors that, in the auditor's professional ~~judgment~~judgement, are significant in directing the engagement team's efforts;
- (d) Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for this entity is relevant; and
- (e) Ascertain the nature, timing and extent of procedures to be performed and the resources necessary to perform the audit, including determining whether experts are needed.

Establishing the scope, timing and direction of the audit need not be a complex or time-consuming exercise. For example, a brief memorandum prepared after the previous audit, based on a review of the working papers and highlighting issues identified in the audit just completed, updated in the current period based on discussions with the owner-manager, can serve as the documented scope, timing and direction for the current audit engagement. Standard audit programmes or

checklists created based on the assumption of few identified controls, as is likely to be the case in a less complex entity, may be used provided that they are tailored to the circumstances of the engagement, including the auditor's risk assessments.

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

5.2.2. The engagement partner and other key members of the engagement team shall be involved in planning the audit.

5.2.3. The auditor shall plan the nature, timing and extent of direction and supervision of engagement team members and review of their work.

5.2.4. The engagement partner shall consider information obtained in the acceptance and continuance process in planning and performing the audit.

5.2.5. When information used to plan and perform the audit has been obtained from the previous experience with the entity, or prior audits, the auditor shall evaluate whether such information remains relevant and reliable as audit evidence in the current period.

5.2.6. The auditor shall update and change the scope, timing and direction as necessary during the audit.

Engagement Team Discussion

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

5.2.7. The engagement partner and other key engagement team members shall discuss the susceptibility of the entity's financial statements to material misstatement, including:

- (a) The application of the applicable financial reporting framework to the entity's facts and circumstances.
- (b) How and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud may occur, and how fraud or error could arise from related party relationships or transactions.

Discussions among the engagement team shall occur setting aside beliefs the engagement team may have that management, and where appropriate, those charged with governance are honest and have integrity.

The engagement team discussion may also include other matters related to the audit such as logistical, operational or other matters (such as when risks of material misstatement may have changed from prior years or matters related to relevant ethical requirements including independence) and the timing of the audit and communications that are required.

5.2.8. When there are engagement team members not involved in the discussion, the engagement partner shall determine which matters are to be communicated to those members.

Using the Work of Management's Expert

5.2.9. If information to be used as audit evidence has been prepared using the work of management's expert, the auditor shall, having regard to the significance of that expert's work for the auditor's purpose:

- (a) Evaluate the competence, capabilities, and objectivity of that expert; and
- (b) Obtain an understanding of the work of that expert.

Evaluating the Competence, Capabilities and Objectivity of a Management's Expert

Competence relates to the nature and level of expertise of the management's expert. Capability relates to the ability of the management's expert to exercise that competence in the circumstances. Objectivity relates to the possible effects that bias, conflict of interest or the influence of others may have on the professional or business ~~judgment~~judgement of the management's expert. Matters relevant to evaluating the competence, capabilities and objectivity of a management's expert may include whether that expert's work is subject to technical performance standards or other professional or industry requirements.

Obtaining an Understanding of the Work of the Management's Expert

When obtaining an understanding of the work of the management's expert, evaluating the agreement between the entity and that expert may assist the auditor in determining the appropriateness of the following for the auditor's purposes:

- *The nature, scope and objectives of that expert's work;*
- *The respective roles and responsibilities of management and that expert; and*
- *The nature, timing and extent of communication between management and that expert, including the form of any report to be provided by that expert.*

Determining Whether to Use the Work of an Auditor's Expert

5.2.10. If expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence, the auditor shall determine whether to use the work of an auditor's expert.

If the preparation of the financial statements involves the use of expertise in a field other than accounting, the auditor, who is skilled in accounting and auditing, may not possess the necessary expertise to audit those financial statements. The auditor's determination of whether to use the work of an auditor's expert and, if so, when and to what extent, assists the auditor in meeting the requirements in paragraphs 3.2.7. and 5.2.1.(e). As the audit progresses, or as circumstances change, the auditor may need to revise earlier decisions about using the work of an auditor's expert.

The auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the auditor's use of the work of an auditor's expert. Nonetheless, if the auditor using the work of an auditor's expert concludes, based on the audit procedures performed and the evidence obtained, that the work of that expert is adequate for the auditor's purposes, the auditor may accept that expert's findings or conclusions in the expert's field as appropriate audit evidence.

5.2.11. The auditor shall consider the following when determining the nature, timing and extent of procedures related to the auditor's expert:

- (a) The nature of the matter to which that expert's work relates;
- (b) The risks of material misstatement in the matter to which that expert's work relates;
- (c) The significance of that expert's work in the context of the audit;
- (d) The auditor's knowledge of and experience with previous work performed by that expert; and

- (e) Whether that expert is subject to the auditor's firm's quality management policies or procedures.

5.2.12. If the auditor is using the work of an auditor's expert, the auditor shall:

- (a) Evaluate whether the auditor's expert has the necessary competence, capabilities and objectivity for the auditor's purposes. In the case of an auditor's external expert, the evaluation of objectivity shall include einquiry regarding interests and relationships that may create a threat to that expert's objectivity;
- (b) Obtain sufficient understanding of the field of expertise of the expert to enable the auditor to determine the nature, scope and objectives of the expert's work for the auditor's purpose, and evaluate the adequacy of that work for the auditor's purpose; and
- (c) Agree, in writing when appropriate, the nature, scope and objectives of the expert's work, the respective roles and responsibilities of the auditor and that expert, the nature, timing and extent of communications and the need for the expert to observe confidentiality requirements.

5.3. Materiality

5.3.1. The auditor shall determine materiality for the financial statements as a whole.

Materiality in the Context of an Audit

The concept of materiality is applied by the auditor in both planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements if any, on the financial statements and in forming an opinion in the auditor's report.

The auditor's determination of materiality is a matter of professional ~~judgment~~judgement, and is affected by the auditor's perception of the financial information needs of users of the financial statements.

The auditor's professional ~~judgment~~judgement about misstatements that will be considered material provides a basis for:

- Determining the nature, timing and extent of procedures to identify and assess risks of material misstatement;*
- Identifying and assessing the risks of material misstatement; and*
- Determining the nature, timing and extent of further audit procedures.*

Use of Benchmarks in Determining Materiality for the Financial Statements as a Whole

A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:

- The elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses)*
- Whether there are items on which the attention of the users tends to be focused;*
- The nature of the entity, where the entity is in its life cycle, and the industry and economic environment in which the entity operates;*
- The entity's ownership structure and the way it is financed. For example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings; and*

- *The relative volatility of the benchmark.*

Examples of benchmarks that may be appropriate, depending on the circumstances of the entity, include categories of reported income such as profit before tax, total revenue, gross profit and total expenses, total equity or net asset value. Profit before tax from continuing operations is often used for profit-oriented entities. When profit before tax from continuing operations is volatile, other benchmarks may be more appropriate, such as gross profit or total revenues. For a not-for-profit organization, a benchmark such as revenue, expenses, assets or equity may be more relevant.

When an entity's profit before tax from continuing operations is consistently nominal, as might be the case for an owner-managed business where the owner takes much of the profit before tax in the form of remuneration, a benchmark such as profit before remuneration and tax may be more relevant.

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.

Considerations Specific to Public Sector Entities

In the case of a public sector entity, legislators and regulators are often the primary users of its financial statements. Furthermore, the financial statements may be used to make decisions other than economic decisions. The determination of materiality for the financial statements as a whole in an audit of the financial statements of a public sector entity is therefore influenced by law, regulation or other authority, and by the financial information needs of legislators and the public in relation to public sector programmes.

In an audit of a public sector entity, total cost or net cost (expenses less revenues or expenditure less receipts) may be appropriate benchmarks for programme activities. Where a public sector entity has custody of public assets, assets may be an appropriate benchmark.

- 5.3.2. The auditor shall also determine the materiality level or levels to be applied to particular classes of transactions, account balances or disclosures if, in the specific circumstances of the entity, there is one or more particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.
- 5.3.3. The auditor shall determine performance materiality for the purposes of assessing the risks of material misstatement, and determining the nature, timing, and extent of further audit procedures.

Planning the audit solely to detect individually material misstatements overlooks the fact that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated, and leaves no margin for possible undetected misstatements. Performance materiality (which, as defined, is one or more amounts) is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

The determination of performance materiality is not a simple mechanical calculation and involves the exercise of professional judgement. It is affected by the auditor's understanding of the entity, updated during the risk identification and assessment; 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.

Clearly Trivial Misstatements

Part 7 requires the auditor to accumulate misstatements identified during the audit, other than those that are clearly trivial. During planning, the auditor may designate an amount below which misstatements of amounts in the individual statements would be clearly trivial, and would not need to be accumulated because the auditor expects that the accumulation of such amounts clearly would not have a material effect on the financial statements.

5.3.4. If the auditor becomes aware of information during the audit that would have caused the auditor to have determined a different amount (or amounts) initially, the auditor shall revise materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures).

5.3.5. If the auditor concludes that a lower materiality for the financial statements as a whole (and, if applicable, materiality level or levels for particular classes of transactions, account balances or disclosures) than that initially determined is appropriate, the auditor shall determine whether it is necessary to revise performance materiality, and whether the nature, timing and extent of the further audit procedures remain appropriate.

5.4. Specific Communication Requirements

5.4.1. The auditor shall communicate with management, and where appropriate, those charged with governance an overview of the planned scope, timing and direction of the audit.

5.5. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

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

Content of this Part

Part 6 contains the requirements relevant to the auditor's responsibility to perform procedures and related activities to:

- Obtain an understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control;
- Identify risks of material misstatement at the financial statement and assertion levels, whether due to fraud or error; and
- Assess inherent risk and control risk.

Appendix 3 illustrates the iterative nature of the auditor's risk identification and assessment.

Scope of this Part

This Part deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements, which provides the basis for the audit procedures undertaken to respond to assessed risks in Part 7. Part 5 sets out the auditor's obligations for planning activities, including the requirements for the engagement team discussion.

6.1. Objectives

- 6.1.1. The objectives of the auditor are to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels, thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement (the assessed risks).

Understanding the entity and its environment, the applicable financial reporting framework and the entity's system of internal control enables the auditor to identify and assess the risks of material misstatement. The auditor's risk identification and assessment process is iterative and dynamic.

6.2. Procedures for Identifying and Assessing Risks and Related Activities

- 6.2.1. The auditor shall design and perform procedures to obtain audit evidence that provides an appropriate basis for:

- (a) The identification and assessment of risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels; and
- (b) The design of further audit procedures.

The auditor uses professional ~~judgment~~judgement to determine the nature and extent of the procedures to be performed, which may vary with the formality of the entity's policies or procedures.

Some less complex entities, and particularly owner-managed entities, may not have established structured processes and systems or may have established processes or systems with limited documentation or a lack of consistency in how they are undertaken. When such systems and processes lack formality, the procedures described in paragraph 6.2.3. are still required.

Designing and performing procedures to obtain audit evidence in a manner that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory may involve obtaining evidence from multiple sources within and

outside the entity. However, the auditor is not required to perform an exhaustive search to identify all possible sources of evidence.

6.2.2. When obtaining audit evidence to identify and assess risks of material misstatement and design further audit procedures, the auditor shall consider information from:

- (a) The acceptance or continuance procedures; and
- (b) When applicable, other engagements performed by the engagement partner for the entity.

6.2.3. The procedures to identify and assess risks of material misstatement shall include:

- (a) ~~E~~inquiries of management, and other appropriate individuals within the entity;
- (b) Analytical procedures; and
- (c) Observation and inspection.

The auditor is not required to perform all of these procedures for each aspect of the auditor's understanding required by this Part.

Analytical procedures performed as a procedure to identify and assess risks of material misstatements help to identify inconsistencies, unusual transactions or events, and amounts, ratios, and trends that indicate matters that may have audit implications. Unusual or unexpected relationships that are identified may assist the auditor in identifying risks of material misstatement, especially risks of material misstatement due to fraud, including those relating to revenue accounts.

Analytical procedures performed as part of the risk identification and assessment may include both financial (e.g., sales price) and non-financial information (e.g., volume of goods sold) and the use of data aggregated at a high level. The auditor may perform a simple comparison of information, such as the change in account balances from balances in prior periods, to identify potential higher risk areas.

Observation and inspection may support, corroborate or contradict ~~e~~inquiries of management and others, and may also provide information about the entity and its environment. Where policies or procedures are not documented, or the entity's controls lack formality, the auditor may still be able to obtain some audit evidence to support the identification and assessment of the risks of material misstatement through observation or inspection of the performance of the control.

Considerations Specific to Public Sector Entities

When making ~~e~~inquiries of those who may have information that is likely to assist in identifying risks of material misstatement, auditors of public sector entities may obtain information from additional sources such as from the auditors that are involved in performance or other audits related to the entity. Procedures performed by auditors of public sector entities to identify and assess risks of material misstatement may also include observation and inspection of documents prepared by management for the legislature, for example documents related to mandatory performance reporting.

Automated Tools and Techniques

If the auditor uses ATT, the auditor may design and perform audit procedures to identify and assess risks of material misstatement on relatively large volumes of data (from the general ledger, sub-ledgers or other operational data) including for analysis, observation or inspection.

6.2.4. In designing and performing procedures to identify and assess risks of material misstatement, the auditor shall consider possible risks of material misstatement arising from:

- (a) Fraud or error;
- (b) Related party relationships and transactions; and
- (c) Events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.

Fraud

Fraudulent financial reporting involves intentional misstatements, including omissions of amounts or disclosures in financial statements to deceive financial statement users. Fraudulent financial reporting often involves management override of controls that otherwise may appear to be operating effectively, such as recording fictitious journal entries close to the end of the financial reporting period.

Misappropriation of assets involves the theft of the entity's assets and is often perpetrated by employees in relatively small and immaterial amounts. However, it can also involve management who are usually more able to disguise or conceal misappropriations in ways that are difficult to detect.

Misappropriation of assets is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorization.

In an LCE there may be different fraud risk factors than in more complex entities. On one hand, management or the owner-manager may be able to exercise more effective oversight than in a more complex entity which may compensate for more limited opportunities for segregation of duties. On the other hand, less segregation of duties and more direct involvement of management or the owner-manager may provide management or the owner-manager with a greater opportunity to override controls and commit fraud. LCEs, including owner-managers may also have different pressures or incentives to commit fraud than management in more complex entities. Appendix 4 sets out fraud risk factors relevant to less complex entities.

Related Parties

In some LCEs, related party transactions between owner-managers and close family members may be common, in particular in closely held entities. These transactions may not be conducted under normal market terms and conditions; for example, some related party transactions may be conducted with no exchange of consideration, or for consideration significantly different from fair value.

Going Concern

Events or conditions that may cast significant doubt on the entity's ability to continue as a going concern of particular relevance to an LCE include the risk that banks and other lenders, close family members or owner-managers may cease to support the entity, as well as the possible loss of a principal supplier, major customer, key employee, or the right to operate under a license, franchise or other legal agreement.

- 6.2.5. If the audit opinion on the prior period's financial statements was modified, the auditor shall evaluate the effect on the current year's financial statements when identifying and assessing risks of material misstatement.

6.3. Understanding Relevant Aspects of the Entity

The auditor's understanding of relevant aspects of the entity, including the entity and its environment, the applicable financial reporting framework and the entity's system of internal

control establishes a frame of reference in which the auditor identifies and assesses the risks of material misstatement, and also informs how the auditor plans and performs further audit procedures.

Enquiries of Management and Others Within the Entity

6.3.1. The auditor shall enquire of management and, where appropriate, those charged with governance, regarding:

- (a) How the entity identifies business risks relevant to the preparation of the financial statements and how they are addressed;
- (b) The risks of fraud in the entity and the controls that management has established to mitigate these risks;
- (c) The nature and extent of management's direct involvement in operations or other activities that may help management to prevent or detect misstatements in accounting information or identify controls that are not operating as intended.
- (d) The identity of the entity's related parties, including:
 - (i) Changes from the prior period;
 - (ii) The nature of the relationships between the entity and these related parties; and
 - (iii) Whether the entity entered into any transactions with these related parties during the period and, if so, the type and purpose of the transactions; and
- (e) Whether the entity is in compliance with laws or regulations that may have an effect on the financial statements, and if there has been any correspondence with relevant licensing or regulatory authorities that may be relevant to the financial statements.
- (f) The basis for the intended use of the going concern basis of accounting, whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and, if so, management's plans to address them.

Enquiries of management and, when applicable, those charged with governance, assist the auditor to identify and assess risks of material misstatement and respond to those risks.

Enquiries about how the entity identifies and assesses its business risks relevant to the preparation of the financial statements may assist the auditor in understanding:

- *Where there are identified business risks;*
- *Whether, and how the entity has responded to those risks;*
- *Whether the risks faced by the entity have been identified, assessed and addressed as appropriate to the nature and circumstances of the entity.*

Enquiries about the risks of material misstatement due to fraud in the entity may assist the auditor in understanding:

- *Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments;*
- *Management's process for identifying and responding to the risks of fraud in the entity, including any specific risks of fraud that management has identified or that have been brought to its attention, or classes of transactions, account balances, or disclosures for which a risk of fraud is likely to exist;*

- Management's communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity.

*E*nquiring about how management performs activities to prevent or detect misstatements in accounting information and identifies controls that are not operating as intended may include ~~e~~nquiring about what information management uses and the basis upon which management considers the information to be sufficiently reliable, as well as *e*nquiring about how deficiencies are remediated. These *e*nquiries assist the auditor to understand whether the other aspects of the entity's system of internal control are present and functioning as appropriate to the entity's circumstances considering the nature and complexity of the entity.

Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future. General purpose financial statements are prepared using the going concern basis of accounting, unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so. When the use of the going concern basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.

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

6.3.2. The auditor shall share relevant information obtained about the entity's related parties with other members of the engagement team.

6.3.3. The auditor shall make *e*nquiries of management, those charged with governance, and as appropriate others within the entity, to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity.

Understanding the Entity and Its Environment

6.3.4. The auditor shall obtain an understanding of:

- The entity's ~~organizational~~ organizational structure, ownership and governance, and business model.
- The industry and other external factors affecting the entity.
- How the entity's financial performance is measured.
- The legal and regulatory framework applicable to the entity, and how the entity is complying with that framework.
- The entity's transactions and other events and conditions that may give rise to the need for, or changes in, accounting estimates to be ~~recognized~~recognised or disclosed.
- Agreements or relationships that may result in ~~unrecognized~~unrecognised liabilities or future commitments.

Understanding the entity's business model helps the auditor to understand the entity's objectives and strategy, and to understand the business risks the entity takes and faces. Understanding the entity's business risks assists the auditor in identifying risks of material misstatement, since most business risks will eventually have financial consequences and, therefore, an effect on the financial statements. When obtaining an understanding of the entity's business model, the auditor may consider how the entity uses IT.

Relevant industry factors include industry conditions such as the competitive environment, supplier and customer relationships, and technological developments. Other external factors

affecting the entity that the auditor may consider include climate-related risks, the general economic conditions, interest rates and availability of financing, and inflation or currency revaluation.

When understanding agreements or relationships that may result in ~~unrecognized~~~~unrecognised~~ liabilities or future commitments the auditor may consider inspecting minutes of meetings and correspondence with legal counsel and inspecting legal expense accounts.

Considerations Specific to Public Sector Entities

Entities operating in the public sector may create and deliver value in different ways to those creating wealth for owners but will still have a 'business model' with a specific objective. Matters public sector auditors may obtain an understanding of that are relevant to the business model of the entity, include:

- Knowledge of relevant government activities, including related ~~program~~~~mes~~.
- ~~Program~~~~me~~ objectives and strategies, including public policy elements.

Understanding the Applicable Financial Reporting Framework

6.3.5. The auditor shall obtain an understanding of:

- (a) The applicable financial reporting framework including, for accounting estimates, the recognition criteria, measurement bases, and the related presentation and disclosure requirements, and how these apply in the context of the nature and circumstances of the entity and its environment.
- (b) The entity's accounting policies and reasons for any changes thereto.

6.3.6. The auditor shall evaluate whether the entity's accounting policies are appropriate and consistent with the applicable financial reporting framework.

Understanding the Entity's System of Internal Control

In LCEs, and in particular owner-managed entities, the way in which the entity's system of internal control is designed, implemented and maintained will vary with the entity's size and complexity. When there are no ~~formalized~~~~formalised~~ processes or documented policies or procedures, the auditor is still required to obtain an understanding of how management, or where appropriate, those charged with governance prevent and detect fraud and error, and use professional ~~judgment~~~~judgement~~ to determine the nature and extent of the procedures to obtain the required understanding.

Considerations Specific to Public Sector Entities

Auditors of public sector entities often have additional responsibilities with respect to internal control, for example, to report on compliance with an established code of practice or reporting on spending against budget. Auditors of public sector entities may also have responsibilities to report on compliance with law, regulation or other authority. As a result, their considerations about the system of internal control may be broader and more detailed.

Understanding the Entity's Control Environment

6.3.7. The auditor shall:

- (a) Obtain an understanding of the control environment relevant to the preparation of the financial statements; and

- (b) Evaluate whether the control environment provides an appropriate foundation for the entity's system of internal control considering the nature and complexity of the entity.

The auditor's understanding may include:

- *How management, and where appropriate, those charged with governance, oversee the entity, demonstrate integrity and ethical values, for example, through communication to employees regarding expectations for business practices and ethical ~~behavior~~behaviour;*
- *The culture of the entity, including whether management supports honesty and ethical ~~behavior~~behaviour;*
- *The entity's assignment of authority and responsibility;*
- *How the entity attracts, develops, and retains competent individuals; and*
- *When applicable, how owner-managers are actively involved in the business and how this may impact the risks arising from management override of controls due to lack of segregation of duties.*

The control environment provides an overall foundation for the operation of the other aspects of the entity's system of internal control, and deficiencies may undermine the rest of the entity's system of internal control. Although it does not directly prevent or detect and correct misstatements, it may influence the effectiveness of other controls in the system of internal control. The control environment includes the governance and management functions and the attitudes, awareness and actions of those charged with governance and management concerning the entity's system of internal control and its importance in the entity.

Because the control environment is foundational to the entity's system of internal control, any deficiencies could have pervasive effects on the preparation of the financial statements. Therefore, the auditor's understanding and evaluation of the control environment affects the auditor's identification and assessment of risks of material misstatement at the financial statement level, and may also affect the identification and assessment of risks of material misstatement at the assertion level, as well as the auditor's responses to the assessed risks.

Some or all aspects of the control environment may not be applicable for an LCE or may be less ~~formalized~~formalised. For example, an LCE may not have a written code of conduct but, instead, may have developed a culture that ~~emphasize~~emphasises the importance of integrity and ethical ~~behavior~~behaviour through oral communication and by management example.

Some entities may be dominated by a single individual who may exercise a great deal of discretion. The actions and attitudes of that individual may have a pervasive effect on the culture of the entity, which in turn may have a pervasive effect on the control environment. Domination of management by a single individual in an LCE does not generally, in and of itself, indicate a failure by management to display and communicate an appropriate attitude regarding internal control and the financial reporting process. In some entities, the need for management ~~authoriz~~ation can compensate for otherwise deficient controls and reduce the risk of employee fraud. However, domination of management by a single individual can be a potential control deficiency since there is an opportunity for management override of controls.

Understanding the Entity's Process to Prepare its Financial Statements

6.3.8. For significant classes of transactions, account balances and disclosures, the auditor shall obtain an understanding of the entity's process to prepare its financial statements including:

- (a) The accounting records and other records that support the classes of transactions, account balances and disclosures in the financial statements;

- (b) How transactions are initiated, and how information about them is recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements;
- (c) How information about events and conditions, other than transactions are identified, processed and disclosed; and
- (d) The entity's resources, including the IT environment, relevant to (a) to (c) above.

Matters the auditor may consider when obtaining an understanding of the entity's process to prepare its financial statements relating to significant classes of transactions, account balances and disclosures include how:

- *The data or information relating to transactions, other events and conditions is processed;*
- *The integrity of that data or information is maintained; and*
- *The information processes, personnel and other resources are used.*

The auditor's understanding may be obtained in various ways and may include:

- *Enquiries of relevant personnel about the procedures used to initiate, record, process and report transactions or about the entity's financial reporting process;*
- *Inspection of policy or process manuals or other documentation of the entity's process to prepare the financial statements;*
- *Observation of the performance of the policies or procedures by entity's personnel; or*
- *Selecting transactions and tracing them through the applicable process to prepare the financial statements (i.e., performing a walk-through).*

LCEs with direct management involvement may not need extensive descriptions of accounting procedures, sophisticated accounting records, or written policies.

Automated Tools and Techniques

The auditor may also use ATT to obtain direct access to, or a digital download from, the databases in the entity's information system that store accounting records of transactions. By applying ATT to this information, the auditor may confirm the understanding obtained about how transactions flow through the information system by tracing journal entries, or other digital records related to a particular transaction, or an entire population of transactions, from initiation in the accounting records through to recording in the general ledger. Analysis of complete or large sets of transactions may also result in the identification of variations from the normal, or expected processing procedures for these transactions, which may result in the identification of risks of material misstatement.

6.3.9. For accounting estimates and related disclosures for significant classes of transactions, account balances or disclosures, the auditor shall obtain an understanding of how management:

- (a) Identifies, selects and applies relevant methods, assumptions and data that are appropriate in the context of the applicable financial reporting framework, including identification of significant assumptions;
- (b) Understands the degree of estimation uncertainty and addresses such uncertainty, including selecting a point estimate and related disclosures for inclusion in the financial statements; and
- (c) Reviews the outcome(s) of previous accounting estimates and responds to the results of that review.

6.3.10. The auditor shall evaluate whether the entity's process to prepare its financial statements, including for accounting estimates, appropriately supports the preparation of its financial statements in accordance with the applicable financial reporting framework.

Understanding the Services Provided by a Service Organization

6.3.11. If the entity uses the services of a service organization and those services are relevant to the entity's process to prepare its financial statements, the auditor's understanding in accordance with paragraph 6.3.8. shall include:

- (a) The nature of the services provided by the service organization and the significance of those services to the entity including the effect thereof on the user entity's system of internal control;
- (b) The nature and materiality of the transactions processed or accounts or financial reporting processes affected by the service organization;
- (c) The degree of interaction between the activities of the service organization and those of the user entity; and
- (d) The relevant contractual terms for the activities undertaken by the service organization.

The auditor's understanding shall be sufficient to provide an appropriate basis for the identification and assessment of the risks of material misstatement.

LCEs may often use external bookkeeping services ranging from the processing of certain transactions (for example, processing of payroll and payment of payroll taxes) and maintenance of their accounting records to the preparation of their financial statements. The use of such a service organization for the preparation of its financial statements does not relieve management of the less complex entity and, where appropriate, those charged with governance of their responsibilities for the financial statements.

The services of a service organization are relevant to the entity's process to prepare its financial statements when those services, and the controls over them, are part of, or affect the process described in paragraph 6.3.8.

The auditor's understanding helps to inform the auditor about the nature and significance of the services provided by the service organization and their effect on the user entity's system of internal control, which affect the nature and extent of work to be performed by the auditor regarding the services provided by a service organization. The significance of the controls of the service organization relative to those of the entity depends on the degree of interaction between the service organization's activities and those of the entity. For example, the service organization may process and account for transactions that are still required to be ~~authorized~~ authorised by the entity, alternatively the entity may rely on such controls being affected at the service ~~organization~~ organisation.

The service organization may have engaged a service auditor to provide a report on the description and design (a type 1 report), or on the description, design and operating effectiveness (a type 2 report), of controls at the service organization. Such reports may provide information for the auditor in obtaining an understanding of the user entity's system of internal control. However, this standard has not been designed for, and therefore does not include requirements to address, the auditor's use of such reports as audit evidence about the design, implementation or operating effectiveness of controls at the service organization.

Understanding the Entity's Control Activities

6.3.12. The auditor shall obtain an understanding of the entity's control activities by identifying controls that address risks of material misstatement at the assertion level as set out below. For each control identified in (a)—(e) below, the auditor shall perform procedures, beyond einquiry, to evaluate whether the control is designed effectively and has been implemented:

- (a) Controls that address risks determined to be significant risks;
- (b) Controls over journal entries, including journal entries to record non-recurring, unusual transactions or adjustments;
- (c) Controls, if any, for which the auditor plans to test the operating effectiveness of controls in determining the nature, timing and extent of substantive testing, including those controls that address risks for which substantive procedures alone are not enough to obtain sufficient appropriate audit evidence; and
- (d) Controls, if any, related to significant transactions and arrangements with related parties, and significant transactions and arrangements outside the normal course of business.
- (e) Controls, if any, in (a) to (d) at the user entity related to the services provided by the service organization, including those that are applied to the transactions processed by the service organization.

The auditor's required understanding of the entity's control activities involves identifying specific controls, as appropriate in the entity's circumstances, and evaluating their design and determining whether the controls have been implemented. Evaluating the design and implementation of controls includes the evaluation of whether the control is designed effectively to address the risk of material misstatement at the assertion level, or effectively designed to support the operation of other controls, and the determination whether the control has been implemented.

This assists the auditor's understanding of management's approach to addressing certain risks, and therefore provides a basis for the design and performance of further audit procedures responsive to these risks even when the auditor does not plan to test the operating effectiveness of identified controls.

Journal Entries

Controls over journal entries are expected to be identified for all audits because the manner in which an entity incorporates information from transaction processing into the general ledger ordinarily involves the use of journal entries, whether standard or non-standard, or automated or manual. The extent to which other controls are identified may vary based on the nature of the entity and the auditor's planned approach to further audit procedures. For example, the entity's information system may not be complex and the auditor may not intend to test the operating effectiveness of controls. Further, the auditor may not have identified any significant risks or any other risks of material misstatement for which it is necessary for the auditor to evaluate the design of controls and determine that they have been implemented. In such an audit, the auditor may determine that there are no identified controls other than the entity's controls over journal entries.

Related Parties

Controls in LCEs are likely to be less formal and such entities may have no documented processes for dealing with related party relationships and transactions. An owner-manager may mitigate some of the risks arising from related party transactions, or potentially increase those risks, through active involvement in all the main aspects of the transactions. For such entities, the auditor may obtain an understanding of the related party relationships and transactions, and any

controls that may exist over these, through einquiry of management combined with other procedures, such as observation of management's oversight and review activities, and inspection of available relevant documentation.

6.3.13. For the controls identified in paragraph 6.3.12. the auditor shall:

- (a) Identify the IT applications and other aspects of the IT environment that are subject to risks arising from the use of IT and what those related risks are;
- (b) Identify the entity's general IT controls that respond to those identified risks; and
- (c) By performing procedures in addition to einquiries, evaluate whether the identified general IT controls are designed effectively and have been implemented.

The auditor's understanding of the entity's process to prepare the financial statements (which may be done by performing walk-through procedures) includes the IT environment relevant to the flows of transactions and processing of information. This is because the entity's use of IT applications or other aspects of the IT environment may give rise to risks arising from the use of IT (i.e., the susceptibility of information processing controls to ineffective design or operation, or risks to the integrity of information).

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. General IT controls support the continued proper operation of the IT environment, including the continued effective functioning of information processing controls and the integrity of information.

Deficiencies Within the Entity's System of Internal Control

6.3.14. The auditor shall 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.

In understanding the entity's system of internal control, the auditor may determine that certain of the entity's policies or procedures are not appropriate to the nature and circumstances of the entity. Such a determination may be an indicator that assists the auditor in identifying deficiencies in internal control. If the auditor has identified one or more deficiencies, the auditor may consider the effect of those deficiencies on the identification and assessment of risks of material misstatement and on the design of further audit procedures.

The auditor uses professional judgment in determining whether a deficiency represents a significant deficiency in internal control.

6.4. Identifying and Assessing the Risks of Material Misstatement

Risks of material misstatement are identified and assessed by the auditor to determine the nature, timing and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence. This evidence enables the auditor to express an opinion on the financial statements at an acceptably low level of audit risk.

6.4.1. The auditor shall identify and assess the risks of material misstatement, due to fraud or error, at:

- (a) The financial statement level. In doing so, the auditor shall determine whether they affect risks at the assertion level and consider the nature and extent of the pervasive effect of identified risks on the financial statements; and

- (b) The assertion level for classes of transactions, account balances, and disclosures. In doing so, the auditor shall:
- (i) Determine the relevant assertions and related significant classes of transactions, account balances and disclosures; and
 - (ii) Assess inherent risk for identified risks of material misstatement at the assertion level by assessing the likelihood and magnitude of misstatement.

Financial Statement Level Risks

Risks of material misstatement at the financial statement level refer to risks that relate pervasively to the financial statements as a whole, and potentially affect many assertions. Risks of this nature are not necessarily risks related to specific assertions at the class of transactions, account balance or disclosure level (e.g., risk of management override of controls).

Assertion Level Risks

In identifying and assessing the risks of material misstatement, the auditor uses assertions to consider the different types of potential misstatements that may occur. Appendix 5 sets out assertions that may be used by the auditor in considering different types of misstatements at the assertion level.

An assertion about a class of transactions, account balance or disclosure is a relevant assertion when it has an identified risk of material misstatement. The determination of whether an assertion is a relevant assertion is made before consideration of any related controls (i.e., the inherent risk) and is based on the auditor's consideration of misstatements that have a reasonable possibility of both occurring (i.e., likelihood), and being material if they were to occur (i.e., magnitude). Significant classes of transactions, account balances and disclosures are those for which there is one or more relevant assertions. Determining relevant assertions and the significant classes of transactions, account balances and disclosures provides a basis for the identification and assessment of risks of material misstatement.

Assessing Inherent Risk

The assessed inherent risk for a particular risk of material misstatement at the assertion level represents a ~~judgment~~judgement within a range, from lower to higher, on the spectrum of inherent risk.

In assessing inherent risk, the auditor uses professional ~~judgment~~judgement in determining the significance of the combination of the likelihood and magnitude of a misstatement on the spectrum of inherent risk. The ~~judgment~~judgement about where in the range inherent risk is assessed may vary based on the nature, size or circumstances of the entity, and takes into account the assessed likelihood and magnitude of the misstatement.

In considering the likelihood of a misstatement, the auditor considers the possibility that a misstatement may occur. In considering the magnitude of a misstatement, the auditor considers the qualitative and quantitative aspects of the possible misstatement (i.e., misstatements in assertions about classes of transactions, account balances or disclosures may be judged to be material due to nature, size or circumstances).

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 (for accounting estimates this is estimation uncertainty); or*
- *Susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect inherent risk.*

The presence of these factors may give rise to higher inherent risk and may be an indication that the ~~ISA for LCE~~ISA (NZ) for LCE is not appropriate for the audit.

When risks of material misstatement relate more pervasively to the financial statements as a whole, and potentially affect many assertions, the risks of material misstatement are assessed at the financial statement level. When assessing risk at the assertion level, the auditor considers the degree to which the risks of material misstatement at the financial statement level affects the assessment of inherent risks for risks of material misstatement at the assertion level.

In identifying and assessing risks of material misstatement, the results of the engagement team discussion and any einquiries relating to fraud and going concern are relevant.

Considerations Specific to Public Sector Entities

In exercising professional ~~judgment~~judgement as to the assessment of the risk of material misstatement, public sector auditors may consider the complexity of the regulations and directives, and the risks of non-compliance with authorities.

- 6.4.2. In identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions, or assertions give rise to such risks.

When identifying and assessing risks of material misstatement due to fraud, the auditor may consider whether unusual or unexpected relationships have been identified in performing analytical procedures, including those related to revenue accounts.

The presumption that there are risks of fraud in revenue recognition may be rebutted. For example, the auditor may conclude, based on the audit evidence obtained, that there is no risk of material misstatement due to fraud relating to revenue recognition in the case where there is a single type of simple revenue transaction, for example, leasehold revenue from a single rental property.

- 6.4.3. In identifying and assessing risks of material misstatement relating to an accounting estimate and related disclosure at the assertion level, the auditor shall consider the degree to which the accounting estimate is subject to estimation uncertainty, and the degree to which the following are affected by complexity, subjectivity, change or management bias:
- (a) The selection and application of the method, the assumptions and data used; and
 - (b) The selection of management's point estimate and related disclosures.

Significant Risks

- 6.4.4. The auditor shall determine whether any of the assessed risks of material misstatement are, in the auditor's professional ~~judgment~~judgement, a significant risk.

The determination of which of the assessed risks of material misstatement are close to the upper end of the spectrum of inherent risk, and are therefore significant risks, is a matter of professional ~~judgment~~judgement, unless the risk is of a type specified to be treated as a significant risk as set out in paragraph 6.4.6. Being close to the upper end of the spectrum of inherent risk will differ

from entity to entity, and will not necessarily be the same for an entity period on period. It may depend on the nature and circumstances of the entity for which the risk is being assessed.

6.4.5. The auditor shall determine whether the assessed risks associated with related party relationships and transactions, and assessed risks relating to accounting estimates are significant risks.

6.4.6. The auditor shall treat the following as significant risks:

- (a) Risk of material misstatement from management override of controls;
- (b) Any other risks of material misstatement due to fraud, including risks that the auditor identified in accordance with paragraph 6.4.2.; or
- (c) Identified significant related party transactions outside the entity's normal course of business.

Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and therefore a significant risk.

Assessing Control Risk

6.4.7. The auditor shall assess control risk if:

- (a) The auditor has determined that substantive procedures alone cannot provide sufficient appropriate audit evidence for any of the risks of material misstatement at the assertion level; or
- (b) The auditor otherwise plans to test the operating effectiveness of controls.

Otherwise, the assessed risk of material misstatement is the same as the assessment of inherent risk.

The auditor's plans to test the operating effectiveness of controls is based on the expectation that controls are operating effectively, and this will form the basis of the auditor's assessment of control risk.

The initial expectation of the operating effectiveness of controls is based on the auditor's evaluation of the design, and the determination of implementation, of the controls identified in paragraphs 6.3.12. and 6.3.13.-(b). Once the auditor has tested the operating effectiveness of the controls in accordance with Part 7, the auditor will be able to confirm the initial expectation about the operating effectiveness of controls. If the controls are not operating effectively as expected, then the auditor will need to revise the control risk assessment.

The auditor's assessment of control risk may be performed in different ways depending on preferred audit techniques or methodologies, and may be expressed in different ways. The control risk assessment may be expressed using qualitative categories (for example, control risk assessed as maximum, moderate, minimum) or in terms of the auditor's expectation of how effective the control(s) is in addressing the identified risk, that is, the planned reliance on the effective operation of controls. For example, if control risk is assessed as maximum, the auditor contemplates no reliance on the effective operation of controls. If control risk is assessed at less than maximum, the auditor contemplates reliance on the effective operation of controls.

Where routine business transactions are subject to highly automated processing with little or no manual intervention, it may not be possible to perform only substantive procedures in relation to the risk. This may be the case in circumstances where a significant amount of an entity's information is initiated, recorded, processed, or reported only in electronic form. In such cases:

- ~~——~~ *The sufficiency and appropriateness of audit evidence usually depend on the effectiveness of controls over its accuracy and completeness.*
- ~~——~~ *The potential for improper initiation or alteration of information to occur and not be detected may be greater if appropriate controls are not operating effectively.*

Evaluation of the Procedures to Identify and Assess Risks of Material Misstatement and Revision of Risk Assessment

6.4.8. The auditor shall evaluate whether the audit evidence obtained from procedures to identify and assess the risks of material misstatement provides an appropriate basis for the identification and assessment of the risks of material misstatement. If not, the auditor shall perform additional procedures until audit evidence has been obtained to provide such a basis. In identifying and assessing the risks of material misstatement, the auditor shall consider all audit evidence obtained from the procedures to identify and assess the risks of material misstatement, whether corroborative or contradictory to assertions made by management.

6.4.9. The auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained. 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, the auditor shall revise the assessment and modify the further planned audit procedures accordingly.

6.4.10. The auditor shall remain alert throughout the audit for audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.

If events or conditions that may cast significant doubt on the entity's ability to continue as a going concern are identified after the auditor's risk assessments are made, the auditor's assessment of the risks of material misstatement may need to be revised.

6.5. Evaluation of the Appropriateness of Using the ~~ISA for LCE~~ISA (NZ) for LCE

6.5.1. Based on the procedures performed to identify and assess the risks of material misstatement, the engagement partner shall evaluate whether the ~~ISA for LCE~~ISA (NZ) for LCE continues to be appropriate for the nature and circumstances of the entity being audited.

The auditor's original determination to use the ~~ISA for LCE~~ISA (NZ) for LCE may change as new information or additional audit evidence is obtained when performing procedures to identify and assess risks of material misstatement. 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~~ISA (NZ) for LCE, the auditor may need to change the original determination to use the ~~ISA for LCE~~ISA (NZ) for LCE, and transition to using the ISAs (NZ) or other applicable standards as appropriate.

6.6. Specific Communication Requirements

6.6.1. The auditor shall communicate with management, and where appropriate, those charged with governance, the significant risks identified by the auditor.

6.7. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

The form and extent of documentation for the identification and assessment of the risks of material misstatement may be simple and relatively brief, and is influenced by:

- *The nature, size and complexity of the entity and its system of internal control.*
- *Availability of information from the entity.*
- *The audit methodology and technology used in the course of the audit.*

It is not necessary to document the entirety of the auditor's understanding of the entity and matters related to it, but rather apply the principles in Part 2.4. and the matters noted below.

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

- 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;
- The names of the identified related parties (including changes from prior period) and the nature of the related party relationships;
- 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 ~~judgment~~judgements made;
- If applicable, the reasons for the conclusion that there is not a risk of material misstatement due to fraud related to revenue recognition;
- 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
- 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~~ISA (NZ) ~~for LCE~~ continues to be appropriate for the nature and circumstances of the entity being audited.

7. Responding to Assessed Risks of Material Misstatement

Content of this Part

Part 7 contains content related to the:

- Design and implementation of overall responses to assessed risks of material misstatement at the financial statement level;
- Design and implementation of responses to the assessed risks of material misstatement at the assertion level (i.e., design and performance of further audit procedures). Further procedures include substantive procedures (tests of detail and substantive analytical procedures) and tests of controls (as appropriate), and are expanded on in this Part; and
- Procedures for specific topics when responding to assessed risks of material misstatement.

Scope of this Part

This Part sets out the specific requirements for obtaining audit evidence through responding to assessed risks of material misstatement. Part 2 also sets out the broad requirements for audit evidence. In complying with the requirements in this Part, the auditor may find it useful to refer to the following that set out relevant matters:

- Fraud – see Part 1.5.
- Laws and regulations – see Part 1.6.
- Related parties – see Part 1.7.
- Information to be used as audit evidence – see Part 2.3.

7.1. Objectives

7.1.1. The objectives of the auditor are to:

- (a) Obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement, through designing and implementing responses to those risks;
- (b) Respond appropriately to risks of material misstatement arising from fraud or suspected fraud;
- (c) Obtain sufficient appropriate audit evidence regarding management's use of the going concern assumption and related disclosures; and
- (d) Respond appropriately to identified or suspected non-compliance with law or regulation that have been identified during the audit.

7.2. Audit Procedures Responsive to the Assessed Risks of Material Misstatement at the Financial Statement Level

7.2.1. The auditor shall design and implement overall responses to address the assessed risks of material misstatement at the financial statement level, whether due to fraud or error.

The auditor's overall responses at the financial statement level, for example, making general changes to the nature, timing or extent of audit procedures, or adjustments to resources assigned or using experts, are based on those risks that relate pervasively to the financial statements as a whole. These may include, for example, risks arising from industry, regulatory and other external factors, or matters related broadly to the entity's basis of accounting or accounting policies.

In particular, the auditor's overall responses also are influenced by the auditor's understanding of the control environment. The control environment provides an overall foundation for the operation of the other aspects of the entity's system of internal control. Although the control environment does not directly prevent, or detect and correct misstatements, it may influence the effectiveness of other controls in the system of internal control. Therefore, an effective control environment may allow the auditor to have more confidence in internal control and the reliability of audit evidence generated internally within the entity.

Deficiencies that have been identified in the control environment when obtaining an understanding of the entity's system of internal control, however, have the opposite effect and may result in the need for more extensive audit evidence from substantive procedures. A weak control environment also impacts the work that may be undertaken at an interim period.

7.2.2. In determining overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level, the auditor shall:

- (a) Evaluate whether the selection and application of accounting policies by the entity, particularly those related to subjective measurements, may be indicative of fraudulent financial reporting resulting from management's effort to manage earnings; and
- (b) Incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures.

Incorporating an element of unpredictability may be achieved by, for example:

- *Performing substantive procedures on selected account balances and assertions not otherwise tested due to their materiality or risk.*
- *Adjusting the timing of audit procedures from that otherwise expected.*
- *Using different sampling methods.*
- *Performing audit procedures at different locations or at locations on an unannounced basis.*

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

7.2.3. In determining overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level, the auditor shall assign and supervise personnel taking account of the knowledge, skill, and ability of the individuals to be given significant engagement responsibilities and the auditor's assessment of the risks of material misstatement due to fraud for the engagement.

7.3. Audit Procedures Responsive to the Assessed Risks of Material Misstatement at the Assertion Level

7.3.1. The auditor shall design and perform further audit procedures whose nature, timing and extent are based on, and responsive to, assessed risks, whether due to fraud or error, at the assertion level.

Further audit procedures comprise tests of controls and substantive procedures. The auditor may choose to perform tests of controls or they may be required in specific circumstances (see paragraph 7.3.2.(d)). Substantive procedures include tests of details and substantive analytical procedures.

Further audit procedures are responsive to the assessed risk of material misstatement at the assertion level, and provide a clear linkage between the auditor's further procedures and the risk

assessment. If the assessed risks of material misstatement are due to fraud risks at the assertion level, the nature, timing and extent of audit procedures may need to be changed to obtain audit evidence that is more relevant and reliable or to obtain additional corroborative information.

The auditor need not design and perform further audit procedures where the assessment of the risk of material misstatement is below the acceptably low level. However, as required by paragraph 7.3.14, irrespective of the assessed risk, the auditor shall perform substantive procedures for each material class of transactions, account balance, and disclosure.

7.3.2. In designing the further audit procedures, the auditor shall:

- (a) Consider the reasons for the assessment given to the risk of material misstatement at the assertion level for each significant class of transactions, account balance, or disclosure, including:
 - (i) The likelihood and magnitude of misstatement due to the characteristics of the significant class of transactions, account balance, or disclosure (that is, the inherent risk); and
 - (ii) Whether the risk assessment takes account of controls that address the risk of material misstatements (that is, the control risk), thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively (where the auditor plans to test the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures);
- (b) Obtain more persuasive audit evidence the higher the auditor's assessment of risk;
- (c) In designing and performing tests of controls, obtain more persuasive audit evidence the greater the reliance the auditor places on the operating effectiveness of controls; and
- (d) If the auditor intends to test the operating effectiveness of controls or when substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level, design and perform tests of controls, to obtain sufficient appropriate audit evidence as to the operating effectiveness of such controls.

In some audits, the auditor may not be able to identify many controls, or the extent of documentation prepared by the entity to which they exist or operate may be limited. In such cases, it may be more efficient for the auditor to perform further audit procedures that are primarily substantive procedures.

When obtaining more persuasive audit evidence because of a higher assessment of risk, the auditor may increase the quantity of the evidence, or obtain evidence that is more relevant or reliable, for example, by placing more emphasis on obtaining third party evidence or by obtaining corroborating evidence from a number of independent sources.

Considerations Specific to Public Sector Entities

For the audits of public sector entities, the audit mandate and any other special auditing requirements may affect the auditor's consideration of the nature, timing and extent of further audit procedures.

7.3.3. When designing tests of controls and tests of details, the auditor shall determine the means of selecting items for testing that are effective in meeting the purpose of the audit procedure.

In selecting items for testing, the auditor is required by paragraph 2.3.1, to determine the relevance and reliability of information to be used as audit evidence; the other aspect of effectiveness (sufficiency) is an important consideration in selecting items to test. The means

available to the auditor for selecting items for testing are selecting all items (100% examination), selecting specific items and audit sampling.

Tests of Controls

- 7.3.4. In designing and performing tests of controls, the auditor shall perform audit procedures in combination with einquiry to obtain audit evidence about the operating effectiveness of controls, including:
- (a) How the controls were applied at relevant times during the period;
 - (b) The consistency with which they were applied; and
 - (c) By whom or by what means they were applied.
- 7.3.5. The auditor shall determine whether the controls to be tested depend on other controls (indirect controls), and, if so, consider whether it is necessary to obtain evidence about the effective operation of the indirect controls.
- 7.3.6. The auditor shall test controls for the period of time, or throughout the period, for which the auditor intends to rely on those controls in order to provide an appropriate basis for the auditor's reliance.
- 7.3.7. If the auditor obtains audit evidence about the operating effectiveness of controls in the interim period, the auditor shall obtain additional audit evidence about any subsequent significant changes and determine the additional audit evidence to be obtained for the remaining period.
- 7.3.8. If the auditor intends to use audit evidence about the operating effectiveness of controls obtained in previous periods, the auditor shall:
- (a) Consider:
 - (i) The effectiveness of the system of internal control;
 - (ii) The risks from the characteristics of the control (e.g., manual or automated);
 - (iii) The effectiveness of general IT controls;
 - (iv) The effectiveness of the control and its application by the entity;
 - (v) Whether the lack of a change in a particular control poses a risk due to changing circumstances; and
 - (vi) The risk of material misstatement and the extent of reliance on the control planned; and
 - (b) Establish the continuing relevance of that evidence by obtaining audit evidence about whether significant changes in those controls have occurred subsequent to the previous audit. If there have been significant changes the auditor shall test the control in the current period, otherwise at least once every third audit.
- 7.3.9. If the auditor intends to rely on a control that is a control over a significant risk, the auditor shall test the control in the current period.
- 7.3.10. When evaluating the operating effectiveness of controls upon which the auditor intends to rely, the auditor shall evaluate whether misstatements that have been detected by substantive procedures indicate that controls are not operating effectively. The absence of misstatements detected by substantive procedures, however, does not provide audit evidence that controls related to the assertion being tested are effective.

7.3.11. If deviations from controls upon which the auditor intends to rely are detected, the auditor shall make specific einquiries to understand these matters and their potential consequences, and shall determine whether:

- (a) The tests of controls provide an appropriate basis for reliance on the controls;
- (b) Additional tests of control are necessary; or
- (c) The risks of material misstatement need to be addressed using substantive procedures.

Substantive Procedures

7.3.12. The auditor's substantive procedures shall include substantive procedures specifically responsive to significant risks. When the response to a significant risk consists only of substantive procedures, those procedures shall include tests of details.

7.3.13. The auditor's substantive procedures shall include audit procedures related to the financial statement closing process, including:

- (a) Agreeing or reconciling information in the financial statements with the underlying accounting records, including agreeing or reconciling information in disclosures, whether such information is obtained from within or outside of the general and subsidiary ledgers; and
- (b) Examining material journal entries and other adjustments made during the course of preparing the financial statements.

7.3.14. Irrespective of the assessed risks, substantive procedures shall be performed for each material class of transactions, account balance, and disclosure.

Paragraph 7.3.14 requires the auditor to design and perform further audit procedures whose nature, timing and extent are based on, and responsive to assessed risks of material misstatement at the assertion level. Because of this, substantive procedures may have already been performed for significant classes of transactions, account balances and disclosures.

Not all assertions within a material class of transactions, account balance or disclosure are required to be tested. Rather, in designing the substantive procedures to be performed, the auditor's consideration of the assertion(s) in which, if a misstatement were to occur, there is a reasonable possibility of the misstatement being material, may assist in identifying the appropriate nature, timing and extent of the procedures to be performed.

7.3.15. If the auditor performed substantive procedures at an interim date, the auditor shall cover the remaining period by performing:

- (a) Substantive procedures, combined with tests of controls for the intervening period; or
- (b) If the auditor determines that it is sufficient, further substantive procedures only, that provide a reasonable basis for extending the audit conclusions from the interim date to the period end.

Substantive Analytical Procedures

7.3.16. If the auditor uses substantive analytical procedures to obtain audit evidence, the auditor shall:

- (a) Determine the suitability of the substantive analytical procedure for the purpose of the test and for the given assertion(s);
- (b) Evaluate the reliability of data from which the auditor's expectation of recorded amounts or ratios is developed, taking account of source, comparability, and nature and relevance of information available, and controls over its preparation;

- (c) Develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify material misstatements;
- (d) Determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation being required; and
- (e) Investigate fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount by enquiring of management and obtaining appropriate audit evidence relevant to management's responses and performing additional audit procedures as necessary in the circumstances.

Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. The application of planned analytical procedures is based on the expectation that relationships among data exist and continue in the absence of known conditions to the contrary. However, the suitability of a particular analytical procedure will depend upon the auditor's assessment of how effective it will be in detecting a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated.

The auditor's determination of the amount of difference from the expectation that can be accepted without further investigation is influenced by materiality, taking account of the possibility that a misstatement, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated. As the assessed risk increases, the amount of difference considered acceptable without investigation decreases in order to achieve the desired level of persuasive evidence.

Automated Tools and Techniques

Analytical procedures can be performed using a number of tools or techniques, which may also be automated. The evolution of technology, coupled with the increase in number and variety of sources of data, may create more opportunities for the auditor to use ATT in performing substantive analytical procedures.

There are countless information sources available (e.g., social media, free access information sources) to the auditor, and some are more reliable than others. The use of ATT to perform substantive analytical procedures allows the auditor to incorporate information from more sources both internal and external to the entity and also to use much greater volumes of data in the analyses. Nonetheless, the auditor's responsibility for addressing the reliability of data used in substantive analytical procedures is unchanged.

Audit Sampling

7.3.17. If the auditor uses audit sampling when responding to assessed risks of material misstatement as a means for selecting items for testing, the auditor shall:

- (a) Consider the purpose of the audit procedures and the characteristics of the population from which the sample will be drawn.
- (b) Determine a sample size sufficient to reduce sampling risk to an acceptably low level.
- (c) Select items in a way that each sampling unit in the population has a chance of selection.
- (d) Perform audit procedures, appropriate to the purpose, on each item selected. If the procedure is not applicable to the selected item, the auditor shall 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 shall 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).

- (e) Investigate the nature and cause of any deviations or misstatements identified and evaluate their possible effect on the purpose of the audit procedure and on other areas of the audit.

Sample Design

When designing an audit sample, the auditor's considerations may include:

- *The purpose of the test, the combination of audit procedures that is likely to best achieve the purpose, what items to select to meet the purpose and the assertion being addressed.*
- *The nature of the audit evidence sought and the possible deviation or misstatement conditions or other characteristics relating to that audit evidence will assist the auditor in defining what constitutes a deviation or misstatement and what population to use for sampling.*

The auditor's considerations of the characteristics of a population may include:

- *Whether the population of items to be tested is appropriate to achieve the test objectives. Sampling will not identify or test items that are not already included within the population. For example, a sample of receivable balances may be used to test the existence of receivables, but such a population would not be appropriate for testing the completeness of receivables.*
- *The size of the population. In some cases, a statistical conclusion may not be drawn if the population to be tested is too small to sample.*

Audit sampling can be applied using either non-statistical or statistical sampling approaches. Statistical conclusions can be drawn from statistical samples. Non-statistical samples may be used in combination with other audit procedures that address the same assertion.

Sample Size

The level of sampling risk that the auditor is willing to accept affects the sample size required. The lower the risk the auditor is willing to accept, the greater the sample size will need to be. Appendix 6 includes examples of factors influencing the sample size for tests of controls and test of details.

Selection of Items for Testing

With statistical sampling, sample items are selected in a way that each sampling unit has a known probability of being selected. With non-statistical sampling, ~~judgment~~ judgement is used to select sample items. It is important that the auditor selects a representative sample, so that bias is avoided, by choosing sample items which have characteristics typical of the population.

The principal methods of selecting samples are the use of random selection, systematic selection and haphazard selection.

7.3.18. In the extremely rare circumstances when the auditor considers a misstatement or deviation discovered in a sample to be an anomaly, the auditor shall obtain a high degree of certainty that such misstatement or deviation is not representative of the population. The auditor shall obtain this degree of certainty by performing additional audit procedures to obtain sufficient appropriate audit evidence that the misstatement or deviation does not affect the remainder of the population.

7.3.19. For tests of details, the auditor shall project misstatements found in the sample to the population.

A misstatement that has been established to be an anomaly need not be projected across the remaining population.

7.3.20. The auditor shall evaluate:

- (a) The results of the sample; and
- (b) Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

For tests of controls, an unexpectedly high sample deviation rate may lead to an increase in the assessed risk of material misstatement, unless further audit evidence substantiating the initial assessment is obtained. For tests of details, an unexpectedly high misstatement amount in a sample may cause the auditor to believe that a class of transactions or account balance is materially misstated, in the absence of further audit evidence that no material misstatement exists. Also, 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.

If the auditor concludes that audit sampling has not provided a reasonable basis for conclusions about the population that has been tested, the auditor may:

- *Request management to investigate misstatements that have been identified and the potential for further misstatements and to make any necessary adjustments; or*
- *Tailor the nature, timing and extent of those further audit procedures to best achieve the required assurance. For example, in the case of tests of controls, the auditor might extend the sample size, test an alternative control or modify related substantive procedures.*

External Confirmations

7.3.21. The auditor shall consider whether external confirmation procedures are to be performed as substantive procedures.

External confirmation procedures frequently are relevant when addressing assertions associated with account balances and their elements, but need not be restricted to these items. For example, the auditor may request external confirmation of the terms of agreements, contracts, or transactions between an entity and other parties. External confirmation procedures also may be performed to obtain audit evidence about the absence of certain conditions.

7.3.22. When using external confirmation procedures, the auditor shall maintain control over:

- (a) Determining the information to be confirmed or requested and selecting the appropriate confirming party;
- (b) Designing the confirmation requests, including determining that requests are properly addressed and contain return information for responses to be sent directly to the auditor; and
- (c) Sending the requests, including follow-up requests when applicable, to the confirming party.

7.3.23. If management refuses to allow the auditor to send a confirmation request, the auditor shall:

- (a) **E**nquire as to management's reasons for the refusal, and seek audit evidence as to their validity and reasonableness;
- (b) Evaluate the implications of management's refusal on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures; and

- (c) Perform alternative audit procedures designed to obtain relevant and reliable audit evidence.

7.3.24. If the auditor concludes that management's refusal to allow the auditor to send a confirmation request is unreasonable, or the auditor is unable to obtain relevant and reliable audit evidence from alternative audit procedures, the auditor shall communicate with those charged with governance. The auditor also shall determine the implications for the audit and the auditor's opinion.¹⁸

7.3.25. If the auditor identifies factors that give rise to doubts about the reliability of the response to a confirmation request, the auditor shall obtain further audit evidence to resolve those doubts. If the auditor determines that a response to a confirmation request is not reliable, the auditor shall evaluate the implications on the assessment of the relevant risks of material misstatement, including the risk of fraud, and on the related nature, timing, and extent of other audit procedures.

7.3.26. In the case of each non-response, the auditor shall perform alternative audit procedures to obtain relevant and reliable audit evidence.

7.3.27. The auditor shall investigate exceptions to determine whether they are indicative of misstatements.

7.3.28. The auditor shall evaluate whether the results of the external confirmation procedures, if any, provide relevant and reliable audit evidence, or whether further audit evidence is necessary.

7.4. Specific Focus Areas

Going Concern

The auditor's responsibilities are to obtain sufficient appropriate audit evidence regarding, and conclude:

- *On the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements; and*
- *Based on the audit evidence obtained, whether a material uncertainty exists about the entity's ability to continue as a going concern.*

These responsibilities exist even if the financial reporting framework used in the preparation of the financial statements does not include an explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern.

7.4.1. The auditor shall evaluate management's assessment of the entity's ability to continue as a going concern.¹⁹

In accordance with the requirements of this Part, the auditor needs to evaluate management's assessment of the entity's ability to continue as a going concern. In many cases, the management of less complex entities may not have prepared a detailed assessment of the entity's ability to continue as a going concern, but instead may rely on in-depth knowledge of the business and anticipated future prospects. In such cases, it may be appropriate to discuss the medium- and long-term financing of the entity with management, provided that management's plans can be corroborated by sufficient documentary evidence and are consistent with the auditor's understanding of the entity. Therefore, the auditor's evaluation of going concern, for example, may be satisfied by discussion, einquiry and inspection of supporting documentation.

¹⁸ For the effect on the auditor's report see Part 9, paragraph 9.5.14.

¹⁹ For the effect on the auditor's report see Part 9, paragraph 9.5.17.

Continued support by owner-managers is often important to a less complex entity's ability to continue as a going concern. Where a LCE is largely financed by a loan from the owner-manager, it may be important that these funds are not withdrawn. Where an entity is dependent on additional support from the owner-manager, the auditor may evaluate the owner-manager's ability to meet the obligation under the support arrangement. In addition, the auditor may request written confirmation of the terms and conditions attaching to such support and the owner-manager's intention or understanding.

7.4.2. [Amended by the NZAuASB]

NZ7.4.2. In evaluating management's assessment of the entity's ability to continue as a going concern, the auditor shall:

- (a) Cover the same period as used by management, as required by the applicable financial reporting framework. If that period is less than twelve months from the date of the ~~financial statements~~ auditor's current report, the auditor shall ask management to extend the period. If management does not make or extend its assessment, the auditor shall consider the implications for the auditor's report.²⁰
- (b) Consider whether management's assessment includes all relevant information of which the auditor is aware of as a result of the audit.

The auditor also remains alert to the possibility that there are known events, scheduled or otherwise, or conditions that will occur beyond the period of assessment used by management that may bring into question management's use of the going concern basis of accounting in preparing the financial statements. The further into the future the events or conditions are, the more significant the going concern issues need to be before the auditor takes further action.

7.4.3. The auditor shall inquire of management as to its knowledge of events or conditions beyond the period of management's assessment that may cast significant doubt on the entity's ability to continue as a going concern.

7.4.4. If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern, the auditor shall obtain sufficient appropriate audit evidence to determine whether a material uncertainty exists through performing additional procedures, including consideration of mitigating factors. These procedures shall include:

- (a) Where management has not yet performed an assessment of the entity's ability to continue as a going concern, requesting management to make its assessment.
- (b) Evaluating management's plans for future actions in relation to its going concern assessment, whether the outcome of these plans is likely to improve the situation, and whether management's plans are feasible in the circumstances.
- (c) Where the entity has prepared a cash flow forecast, and analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management's plans for future actions:
 - (i) Evaluating the reliability of the underlying data generated to prepare the forecast; and
 - (ii) Determining whether there is adequate support for the assumptions underlying the forecast.
- (d) Considering whether any additional facts or information have become available since the date on which management made its assessment.

²⁰ For the effect on the auditor's report see Part 9, paragraph 9.5.20.

A material uncertainty exists when the magnitude of its potential impact and likelihood of occurrence is such that, in the auditor's professional ~~judgment~~judgement, appropriate disclosure of the nature and implications of the uncertainty is, for a fair presentation framework, necessary for the fair presentation of the financial statements or, for a compliance framework, necessary for the financial statements not to be misleading.

7.4.5. If there is significant delay in the approval of the financial statements by management or those charged with governance after the date of the financial statements, the auditor shall ~~e~~inquire as to the reasons for the delay. If the auditor believes that the delay could be related to events or conditions relating to the going concern assessment, the auditor shall perform additional audit procedures as necessary, as well as consider the effect on the auditor's conclusion regarding the existence of a material uncertainty.

Management Override of Controls

7.4.6. The auditor shall design and perform audit procedures to:

- (a) Test the appropriateness of manual and automated journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements, including:
 - (i) Making ~~i~~enquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments;
 - (ii) Selecting journal entries and other adjustments made at the end of a reporting period; and
 - (iii) Considering the need to test journal entries and other adjustments throughout the period.
- (b) Review accounting estimates for biases and evaluate whether the circumstances producing the bias, if any, represent a risk of material misstatement due to fraud. In performing the review, the auditor shall:
 - (i) Evaluate whether the ~~judgment~~judgements and decisions made by management indicate a possible bias on the part of the entity's management, even if they are individually reasonable, that may represent a risk of material misstatement due to fraud. If so, the auditor shall ~~re~~-evaluate the accounting estimates taken as a whole; and
 - (ii) Perform a retrospective review of management ~~judgment~~judgements and assumptions related to significant accounting estimates reflected in the financial statements of the prior year.
- (c) For significant unusual transactions outside the normal course of business for the entity or that otherwise appear to be unusual, evaluate whether the business rationale (or the lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.
- (d) Respond to the identified risks of management override of controls to the extent not already addressed by (a) to (c).

Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and therefore a significant risk.

Material misstatement of financial statements due to fraud often involves the manipulation of the financial reporting process by recording inappropriate or ~~unauthorized~~unauthorised journal

entries. This may occur throughout the year or at period end, or both, or by management making adjustments to amounts reported in the financial statements that are not reflected in journal entries, such as through reclassifications.

Automated Tools and Techniques

In manual general ledger systems, non-standard journal entries may be identified through inspection of ledgers, journals, and supporting documentation. When automated procedures are used to maintain the general ledger and prepare financial statements, such entries may exist only in electronic form and may therefore be more easily identified through the use of ATT.

Related Parties

7.4.7. The auditor shall design and perform further audit procedures to obtain sufficient appropriate audit evidence about the assessed risks of material misstatement associated with related party relationships and transactions, including inspecting:

- (a) Bank and legal confirmations obtained as part of the auditor's procedures;
- (b) Minutes of meetings of shareholders and of those charged with governance; and
- (c) Such other records or documents as the auditor considers necessary in the circumstances of the entity.

7.4.8. If the auditor identifies arrangements or information that suggests the existence of related party relationships or transactions that management has not previously identified or disclosed to the auditor, the auditor shall determine whether the underlying circumstances confirm the existence of those relationships or transactions.

7.4.9. If the auditor identifies related parties or significant related party transactions that management has not previously identified or disclosed to the auditor, the auditor shall:

- (a) Where the applicable financial reporting framework establishes related party requirements:
 - (i) Request management to identify all transactions with the newly identified related parties for the auditor's further evaluation;
 - (ii) Enquire as to why the entity's controls over related party relationships and transactions failed to enable the identification or disclosure of the related party relationships or transactions;
- (b) Perform appropriate substantive audit procedures for such newly identified related parties or significant related party transactions;
- (c) Reconsider the risk that other related parties or significant related party transactions may exist that management has not previously identified or disclosed to the auditor, and perform additional audit procedures as necessary; and
- (d) If the non-disclosure by management appears intentional (and therefore indicative of a risk of material misstatement due to fraud), evaluate the implications for the audit.

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

7.4.10. If the auditor identifies related parties or significant related party transactions that management has not previously identified or disclosed to the auditor, the auditor shall promptly communicate the relevant information to the other members of the engagement team.

7.4.11. For identified significant related party transactions outside of the entity's normal course of business the auditor shall:

- (a) Inspect the underlying contracts or agreements, if any, and evaluate whether:
 - (i) The business rationale (or lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets;
 - (ii) The terms of transactions are consistent with management's explanations; and
 - (iii) The transactions have been appropriately accounted for, presented and disclosed in accordance with the applicable financial reporting framework.
- (b) Obtain audit evidence that transactions have been appropriately ~~authorized~~authorised and approved.

7.4.12. If the auditor identifies significant transactions outside the entity's normal course of business, the auditor shall ~~e~~inquire of management about the nature of these transactions and whether related parties could be involved.

7.4.13. If management has made an assertion in the financial statements to the effect that a related party transaction was conducted on terms equivalent to those prevailing in an arm's length transaction, the auditor shall obtain sufficient appropriate audit evidence about the assertion.

Accounting Estimates

7.4.14. The auditor shall design and perform further audit procedures related to accounting estimates to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement at the assertion level, including for related disclosures.

7.4.15. The auditor's further audit procedures to respond to assessed risks of material misstatement at the assertion level relating to an accounting estimate shall include one or more of the following approaches:

- (a) Obtaining audit evidence from events occurring up to the date of the auditor's report (see paragraph 7.4.16.).
- (b) Testing how management made the accounting estimate (see paragraphs 7.4.17.–7.4.18.).
- (c) Developing an auditor's point estimate or range (see paragraph 7.4.19.).

Given the nature of many accounting estimates for an LCE, the final outcome of an accounting estimate may be known before the date of the auditor's report. In these circumstances, audit evidence obtained from events occurring up to the date of the auditor's report may provide sufficient appropriate audit evidence to address the assessed risks of material misstatement. For some accounting estimates, however, events occurring up to the date of the auditor's report may not provide sufficient appropriate audit evidence about whether the accounting estimate is reasonable or misstated (e.g., when events or conditions develop only over an extended period). In these circumstances, the auditor's further audit procedures include the approaches in (b) or (c).

Obtaining Audit Evidence from Events Occurring Up to the Date of the Auditor's Report.

7.4.16. When the auditor's further audit procedures include obtaining audit evidence from events occurring up to the date of the auditor's report, the auditor shall evaluate whether the audit evidence is sufficient and appropriate, taking into account any changes in circumstances and other relevant conditions between the event and the measurement date that may affect the relevance of such evidence.

Testing How Management Made the Accounting Estimate

7.4.17. When testing how management made the accounting estimate, the auditor's further audit procedures shall address whether:

- (a) The method selected is appropriate;
- (b) The significant assumptions and data are consistent and appropriate, and their integrity maintained in applying the method;
- (c) Changes from prior periods in the method, significant assumptions and data are appropriate;
- (d) Management has the intent to carry out specific courses of actions;
- (e) The ~~judgment~~judgements made in selecting the method, significant assumptions and data, give rise to indicators of possible management bias. When indicators of possible management bias are identified, the auditor shall evaluate the implications for the audit. Where there is intention to mislead, management bias is fraudulent in nature;
- (f) The data is relevant and reliable in the circumstances; and
- (g) Calculations are mathematically accurate and whether judgements have been applied consistently.

Method, Significant Assumptions and Data

Relevant considerations for the auditor regarding the appropriateness of the method, significant assumptions and data in the context of the applicable financial reporting framework, and, if applicable, the appropriateness of changes from the prior period may include:

- *Management's rationale for the selection of the method, assumption and data;*
- *Whether the method, assumption and data are appropriate in the circumstances given the nature of the accounting estimate, the requirements of the applicable financial reporting framework, and the business, industry and environment in which the entity operates;*
- *Whether a change from prior periods in selecting a method, assumption or data is based on new circumstances or new information. When it is not, the change may not be reasonable nor in compliance with the applicable financial reporting framework. Arbitrary changes in an accounting estimate may give rise to material misstatements of the financial statements or may be an indicator of possible management bias.*
- *When management has determined that different methods result in a range of significantly different estimates, how management has investigated the reasons for these differences.*
- *Whether the significant assumptions are inconsistent with each other and with those used in other accounting estimates.*

7.4.18. The auditor's further audit procedures shall address whether, in the context of the applicable financial reporting framework, management has taken appropriate steps to understand estimation uncertainty and address estimation uncertainty by selecting appropriate point estimates and developing related disclosures. When management has not undertaken appropriate steps, the auditor shall:

- (a) Request management to perform additional procedures to understand estimation uncertainty or to address it by reconsidering the selection of management's point estimate or considering providing additional disclosures related to the estimation uncertainty; and

- (b) If the auditor determines that management's response to the auditor's request does not sufficiently address estimation uncertainty, to the extent practicable, develop an auditor's point estimate or range.

When the applicable financial reporting framework does not specify how to select a point estimate from among reasonably possible outcomes or does not require specific disclosures, the exercise of ~~judgment~~judgement by management is an important consideration for the auditor regarding the appropriateness of the point estimate selected and the related disclosures.

Matters that may be relevant for the auditor regarding management's disclosures about estimation uncertainty include the requirements of the applicable financial reporting framework, which may require disclosures:

- *That describe the amount as an accounting estimate and explain the nature and limitations of the process for making it; and*
- *About material accounting policy information related to accounting estimates, which may include significant or critical management ~~judgment~~judgements as well as significant forward-looking assumptions or other sources of estimation uncertainty.*

Developing an Auditor's Point Estimate or Range

7.4.19. When the auditor develops a point estimate or range to evaluate management's point estimate, the auditor's further audit procedures shall include audit procedures to:

- (a) Evaluate whether the methods, assumptions or data used are appropriate in the context of the applicable financial reporting framework; and
- (b) Determine that the range includes only amounts that are supported by sufficient appropriate audit evidence.

The auditor's decision as to whether to develop a point estimate rather than a range may depend on the nature of the accounting estimate and the auditor's professional ~~judgment~~judgement in the circumstances. For example, the nature of the accounting estimate may be such that there is expected to be less variability in the reasonably possible outcomes. In these circumstances, developing a point estimate may be an effective approach, particularly when it can be developed with a higher degree of precision.

The requirement for the auditor to determine that the range includes only amounts that are supported by sufficient appropriate audit evidence does not mean that the auditor is expected to obtain audit evidence to support each possible outcome in the range individually. Rather, the auditor is likely to obtain evidence to determine that the points at both ends of the range are reasonable in the circumstances, thereby supporting that amounts falling between those two points also are reasonable.

Inventory

7.4.20. If inventory is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of inventory by:

- (a) Unless impracticable, attendance at physical inventory counting, to:
- (i) Evaluate management's instructions and procedures for recording and controlling the results of the entity's physical inventory counting;
 - (ii) Observe the performance of management's count procedures;
 - (iii) Inspect the inventory; and

- (iv) Perform test counts;
- (b) Performing audit procedures over the entity's final inventory records to determine whether they accurately reflect actual inventory count results; and
- (c) If the physical inventory counting is at a date other than the date of the financial statements, performing audit procedures to obtain audit evidence about whether changes in inventory between the count date and the date of the financial statements are properly recorded.

7.4.21. If the auditor has not attended the inventory count due to unforeseen circumstances, the auditor shall make or observe some physical counts on an alternative date, and perform audit procedures on intervening transactions. If attendance at physical inventory counting is impracticable, the auditor shall perform alternative audit procedures to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory, or if not possible, determine the effect on the auditor's report.²¹

In some cases, attendance at physical inventory counting may be impracticable. This may be due to factors such as the nature and location of the inventory, for example, where inventory is held in a location that may pose threats to the safety of the auditor. The matter of general inconvenience, difficulty, time, or cost involved, however, are not sufficient to support a decision by the auditor that attendance is impracticable. In some cases where attendance is impracticable, alternative audit procedures, for example, inspection of documentation of the subsequent sale of specific inventory items acquired or purchased prior to the physical inventory counting, may provide sufficient appropriate audit evidence about the existence and condition of inventory. In other cases, however, it may not be possible to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory by performing alternative audit procedures. In such cases, the auditor is required to modify the opinion in the auditor's report as a result of the scope limitation.

7.4.22. If inventory under the custody and control of a third party is material to the financial statements, the auditor shall obtain sufficient appropriate audit evidence regarding the existence and condition of that inventory through confirmation as to the quantities and condition, or performing inspection or other audit procedures appropriate in the circumstances.

Litigation and Claims

7.4.23. The auditor shall design and perform further audit procedures in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement, including:

- (a) ~~E~~nquiry of management and, where applicable, others within the entity, including in-house legal counsel;
- (b) Inspecting minutes of meetings of those charged with governance and correspondence between the entity and its external legal counsel; and
- (c) Inspecting legal expense accounts.

7.4.24. If the auditor assesses a risk of material misstatement regarding litigation or claims that have been identified, or when audit procedures performed indicate that other material litigation or claims may exist, the auditor shall, in addition to the procedures required by this standard, seek direct communication with the entity's external legal counsel. The auditor shall do so through a letter of ~~i~~enquiry, prepared by management and sent by the auditor, requesting the entity's external legal counsel to communicate directly with the auditor.²²

²¹ For the effect on the auditor's report see Part 9, paragraph 9.5.15.

²² For the effect on the auditor's report see Part 9, paragraph 9.5.14.

7.4.25. The auditor shall modify the opinion in the auditor's report,²³ if:

- (a) Management refuses to give the auditor permission to communicate or meet with the entity's external legal counsel, or the entity's external legal counsel refuses to respond appropriately to the letter of enquiry, or is prohibited from responding; and
- (b) The auditor is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures.

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

7.4.26. The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally ~~recognized~~recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements.²⁴

7.4.27. If the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws or regulations, the auditor shall:

- (a) Understand the nature and circumstances, and obtain further information necessary to evaluate the possible effect on the financial statements;
- (b) Discuss the non-compliance with management, and where appropriate, those charged with governance, unless prohibited to do so by law or regulation;
- (c) If sufficient information about suspected non-compliance cannot be obtained, evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion; and
- (d) 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.²⁵

Using the Services of a Service ~~Organization~~Organisation

7.4.28. If the entity is using the services of a service ~~organization~~organisation, the auditor shall:

- (a) Determine whether sufficient appropriate audit evidence concerning the relevant financial statement assertions is available at the entity; and, if not,
- (b) Perform further audit procedures to obtain sufficient appropriate audit evidence.

To obtain sufficient appropriate audit evidence, the following procedures may be considered by the auditor:

- *Inspect records and documents held by the user entity;*
- *Inspect records and documents held by the service ~~organization~~organisation;*
- *Obtain confirmations of balances and transactions from the service ~~organization~~organisation in instances where the user entity maintains its own independent records of balances and transactions.*

Using the Work of Management's Expert

7.4.29. If information to be used as audit evidence has been prepared using the work of management's expert, the auditor shall, having regard to the significance of that expert's work for the auditor's purpose, evaluate the appropriateness of the expert's work as audit evidence for the relevant assertion.

²³ For the effect on the auditor's report see Part 9, paragraph 9.5.16.

²⁴ For the effect on the auditor's report see Part 9, paragraph 9.5.10.

²⁵ For the effect on the auditor's report see Part 9, paragraphs 9.5.11., 9.5.12. and 9.5.13.

Considerations when evaluating the appropriateness of the management's expert's work may include:

- *The relevance and reasonableness of that expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial statements;*
- *If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods;*
- *If that expert's work involves significant use of source data, the relevance, completeness, and accuracy of that source data; and*
- *If that expert's work involves the use of information from an external information source, the relevance and reliability of that information.*

Using the Work of an Auditor's Expert

7.4.30. When the auditor has determined to use the work of an auditor's expert, the auditor shall evaluate the adequacy of the auditor's expert's work, including:

- (a) The relevance and reasonableness of that expert's findings or conclusions, and their consistency with other audit evidence;
- (b) If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods in the circumstances; and
- (c) If that expert's work involves the use of source data that is significant to that expert's work, the relevance, completeness, and accuracy of that source data.

7.4.31. If the auditor determines that the work of the auditor's expert is not adequate for the auditor's purposes, the auditor shall agree on further work to be done by that expert or perform additional audit procedures appropriate to the circumstances.

7.5. Accumulation of Misstatements

7.5.1. The auditor shall accumulate misstatements identified during the audit, other than those that are clearly trivial.

Misstatements that are clearly trivial will be of a wholly different (smaller) order of magnitude, or of a wholly different nature than those that would be determined to be material, and will be misstatements that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any criteria of nature, size or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the misstatement is considered not to be clearly trivial.

7.5.2. The auditor shall request management to correct all misstatements accumulated during the audit.

7.5.3. If, at the auditor's request, management has examined a class of transactions, account balance or disclosure and corrected misstatements that were detected, the auditor shall perform additional audit procedures to determine whether misstatements remain.

Such a request may be made, for example, based on the auditor's projection of misstatements identified in an audit sample to the entire population from which it was drawn.

7.5.4. If the auditor identifies a misstatement during the audit, the auditor shall evaluate whether the misstatement is indicative of fraud. If there is such an indication, the auditor shall determine the implications on other aspects of the audit, including on the identified and assessed risks of material misstatement and the reliability of management representations.

Since fraud involves incentive or pressure to commit fraud, a perceived opportunity to do so or some rationalization of the act, an instance of fraud is unlikely to be an isolated occurrence. Accordingly, misstatements, such as numerous misstatements even though the cumulative effect is not material, may be indicative of a risk of material misstatement due to fraud.

7.5.5. If the auditor identifies a misstatement that may be the result of fraud, and suspects that management is involved, the auditor shall:

- (a) Re-evaluate the risks of material misstatement due to fraud and the auditor's responses thereto; or
- (b) Consider whether circumstances or conditions indicate possible collusion involving employees, management or third parties when reconsidering the reliability of evidence previously obtained.

The implications of identified or suspected fraud depends on the circumstances. For example, an otherwise insignificant fraud may be significant if it involves senior management. In such circumstances, the reliability of evidence previously obtained may be called into question, since there may be doubts about the completeness and truthfulness of representations made and about the genuineness of accounting records and documentation. There may also be a possibility of collusion involving employees, management or third parties.

7.5.6. The auditor shall determine whether the scope, timing and direction of the audit needs to be revised if:

- (a) The nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements may exist that, when aggregated with misstatements accumulated during the audit, could be material; and
- (b) The aggregate of misstatements accumulated during the audit approaches materiality.

7.6. Specific Communication Requirements

7.6.1. On a timely basis, the auditor shall communicate:

- (a) To those charged with governance, in writing, significant deficiencies in the entity's system of internal control identified during the audit.
- (b) To management:
 - (i) In writing, matters that have been communicated to those charged with governance (unless it would be inappropriate to communicate directly with management in the circumstances); and
 - (ii) Other deficiencies in internal control identified that have not been communicated but are of sufficient importance to merit management's attention.

7.6.2. In respect of communication of significant deficiencies to those charged with governance, the auditor shall include a description and explanation of the potential impact of the deficiencies, and sufficient information to understand the context of the communication.

In describing the context of the auditor's communication, the auditor may explain that:

- *The purpose of the audit was for the auditor to express an opinion on the financial statements;*
- *The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and*

- *The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.*

7.6.3. In communicating with management and, where appropriate, those charged with governance, the auditor shall consider if there are any matters to communicate regarding accounting estimates. In doing so, the auditor shall consider whether the reasons given to the risks of material misstatement relate to estimation uncertainty, or the effects of complexity, subjectivity, change, or management bias in making accounting estimates and related disclosures.

7.7. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

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

- The overall responses to the assessed risks of material misstatement at the financial statement level;
- The linkage between the procedures performed and the assessed risks at the assertion level;
- The results of the audit procedures, including the conclusions where these are not otherwise clear;
- The results of audit procedures designed to address the risk of management override of controls;
- All misstatements accumulated during the audit and whether they have been corrected; and
- 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:

- The results of discussion with management, and where appropriate, those charged with governance and others; including how the matter has been responded to; and
- The audit procedures performed, the significant professional ~~judgment~~judgements made, and the conclusions reached thereon.

7.7.4. In respect of accounting estimates, the auditor shall document significant ~~judgment~~judgements 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

Content of this Part

Part 8 sets out the requirements for:

- Evaluating corrected and uncorrected misstatements identified during the audit.
- Evaluating subsequent events.
- Concluding activities, including the related evaluations.
- Concluding on going concern and related disclosures.
- Obtaining written representations and performing concluding analytical procedures.

Scope of this Part

The evaluations performed and the conclusions reached will form the basis for the auditor's opinion in Part 9.

8.1. Objectives

8.1.1. The objectives of the auditor are to:

- (a) Evaluate, the effect of identified misstatements on the audit and the effect of any uncorrected misstatements on the financial statements;
- (b) Conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern; and
- (c) Conclude on whether sufficient appropriate audit evidence has been obtained on which to base the auditor's opinion.

8.2. Evaluation of Misstatements Identified During the Audit

8.2.1. If management refuses to correct some or all of the misstatements communicated by the auditor, the auditor shall obtain an understanding of management's reasons for not making the corrections and shall take that understanding into account when evaluating whether the financial statements as a whole are free from material misstatement.

8.2.2. Prior to evaluating the effect of uncorrected misstatements, the auditor shall reassess materiality to confirm whether it remains appropriate in the context of the entity's actual financial results.

8.2.3. The auditor shall determine whether uncorrected misstatements are material, individually or in aggregate, by considering the:

- (a) Nature and size of the misstatements, both in relation to particular classes of transactions, account balances or disclosures and the financial statements as a whole, and the particular circumstances of their occurrence; and
- (b) Effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.

8.3. Analytical Procedures that Assist When Forming an Overall Conclusion

8.3.1. The auditor shall design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are

consistent with the auditor's understanding of the entity, and to identify any indications of a previously unidentified risk of material misstatement due to fraud.

8.3.2. The auditor shall investigate fluctuations or relationships that are inconsistent with other relevant information obtained during the course of the audit, by ~~e~~inquiring of management and performing other audit procedures as necessary in the circumstances.

8.4. Subsequent Events

Financial statements may be affected by certain events that occur after the date of the financial statements. Many financial reporting frameworks specifically refer to such events. Such financial reporting frameworks ordinarily identify two types of events:

- *Those that provide evidence of conditions that existed at the date of the financial statements; and*
- *Those that provide evidence of conditions that arose after the date of the financial statements.*

The auditor is not, however, expected to perform additional procedures on matters to which previously applied audit procedures have provided satisfactory conclusions.

Events Occurring Between the Date of the Financial Statements and the Date of the Auditor's Report

8.4.1. The auditor shall perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified.

8.4.2. The auditor shall perform those procedures in accordance with paragraph 8.4.1. for the period from the date of the financial statements to the date of the auditor's report, or as near as practicable thereto, including:

- (a) Obtaining an understanding of any procedures management has established to ensure that subsequent events are identified.
- (b) ~~E~~inquiring of management, and where appropriate, those charged with governance, as to whether any subsequent events have occurred that may affect the financial statements.
- (c) Reading minutes of meetings of the owners, management and those charged with governance held after the balance sheet date and ~~e~~inquiring about matters discussed at any such meetings for which minutes are not yet available.
- (d) Reading the entity's monthly or quarterly financial information, if available.

8.4.3. If the auditor has identified events that require adjustment to the financial statements or disclosures therein to comply with the entity's applicable financial reporting framework when performing the procedures in paragraphs 8.4.1. and 8.4.2, the auditor shall determine whether each such event is appropriately reflected in the financial statements.

Facts Which Become Known to the Auditor After the Date of the Auditor's Report but Before the Date the Financial Statements Are Issued

8.4.4. The auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, if the auditor becomes aware of facts or events that, had it been known to the auditor at the date of the auditor's report but before the financial statements are issued, may have caused the auditor to amend the auditor's report, the auditor shall discuss with management, and where appropriate, those charged with governance, and

determine whether the financial statements need amendment and, if so, ~~e~~inquire how management intends to address the matter.

8.4.5. If management amends the financial statements, the auditor shall carry out the audit procedures necessary in the circumstances on the amendment, including extending the audit procedures performed to the date of the new auditor's report and providing a new auditor's report on the amended financial statements.

8.4.6. In jurisdictions where management is not required by law, regulation or the financial reporting framework to issue amended financial statements, the auditor need not provide an amended or new auditor's report. However, if management does not amend the financial statements in circumstances where the auditor believes they need to be amended, then the auditor shall:

- (a) If the auditor's report has not yet been provided to the entity modify the opinion and then provide the auditor's report;²⁶ or
- (b) If the auditor's report has already been provided to the entity, notify management and those charged with governance not to issue the financial statements to third parties before the necessary amendments have been made. If the financial statements are nevertheless subsequently issued without the necessary amendments, the auditor shall take appropriate action to seek to prevent reliance on the auditor's report.

Facts Which Become Known to the Auditor After the Financial Statements Have Been Issued

8.4.7. ~~[Amended by the NZAuASB]~~

~~NZ8.4.7.~~ After the financial statements have been issued, the auditor has no obligation to perform any audit procedures regarding such financial statements. However, if, after the financial statements have been issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:

- (a) Discuss the matter with management and, where appropriate, those charged with governance ~~within a reasonable period of time;~~
- (b) Determine whether the financial statements need amendment; and, if so,
- (c) ~~E~~inquire how management intends to address the matter in the financial statements.

8.4.8. If management amends the financial statements, the auditor shall:

- (a) Carry out the audit procedures necessary in the circumstances on the amendment, including:
 - (i) Extending the audit procedures referred to in paragraphs 8.4.1. and 8.4.2. to the date of the new auditor's report, and date the new auditor's report no earlier than the date of approval of the amended financial statements; and
 - (ii) Providing a new auditor's report²⁷ on the amended financial statements; and
- (b) Review the steps taken by management to ensure that anyone in receipt of the previously issued financial statements together with the auditor's report thereon is informed of the situation.

8.4.9. If management does not take the necessary steps to ensure that anyone in receipt of the previously issued financial statements is informed of the situation and does not amend the

²⁶ For the effect on the auditor's report see Part 9, paragraph 9.5.21.

²⁷ For the effect on the auditor's report see Part 9, paragraph 9.6.7.

financial statements in circumstances where the auditor believes they need to be amended, the auditor shall take appropriate action to seek to prevent reliance on the auditor's report.

8.5. The Auditor's Evaluations and Other Activities to Support the Auditor's Conclusion

Evaluations Required

8.5.1. Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate whether the assessments of the risks of material misstatement at the financial statement and assertion levels remain appropriate.

An audit of financial statements is a cumulative and iterative process. As the auditor performs planned audit procedures, the audit evidence obtained may cause the auditor to modify the nature, timing or extent of planned audit procedures. Information may come to the auditor's attention that differs significantly from the information on which the risk assessment was based. In such circumstances, the auditor may need to re-evaluate the planned audit procedures, based on the revised consideration of assessed risks for all or some of the classes of transactions, account balances, or disclosures and related assertions.

The auditor may also consider whether such information changes the auditor's determination about the appropriateness of use of the ~~ISA for LCE~~ ISA (NZ) for LCE for the audit, which may necessitate a modification to the terms of engagement.

8.5.2. For accounting estimates, the auditor shall evaluate, based on the audit procedures performed and audit evidence obtained, whether:

- (a) The assessments of the risks of material misstatement at the assertion level remain appropriate, including when indicators of possible management bias have been identified; and
- (b) Management's decisions about the recognition, measurement, presentation, and disclosure of accounting estimates in the financial statements are reasonable in the context of the applicable financial reporting framework.

8.5.3. The auditor shall evaluate whether two-way communication between the auditor and those charged with governance has been adequate for the purpose of the audit. If it has not, the auditor shall evaluate the effect, if any, on the audit and take action as appropriate.

For example, the original risk assessments may need to be revised, the auditor's opinion may need to be modified on the basis of a scope limitation or other actions may need to be taken as appropriate.

8.5.4. The auditor shall perform audit procedures to evaluate whether the overall presentation of the financial statements is in accordance with the applicable financial reporting framework. In making this evaluation, the auditor shall consider whether the financial statements are presented in a manner that reflects the appropriate:

- (a) Classification and description of financial information and the underlying transactions, events and conditions; and
- (b) Presentation, structure and content of the financial statements.

Concluding

8.5.5. The auditor shall conclude whether sufficient appropriate audit evidence has been obtained. In forming an opinion, the auditor shall consider all relevant audit evidence, regardless of whether it appears to be corroborative or contradictory.

8.5.6. If the auditor has not obtained sufficient appropriate audit evidence as to a relevant assertion, the auditor shall attempt to obtain additional audit evidence. If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall express a qualified opinion or disclaim an opinion on the financial statements.²⁸

8.5.7. The auditor shall evaluate whether sufficient appropriate audit evidence has been obtained regarding, and shall conclude on, the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements.²⁹

8.5.8. The auditor shall conclude, based on the audit evidence obtained, whether in the auditor's professional ~~judgment~~judgement, a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.³⁰

8.5.9. If the auditor concludes that management's use of the going concern basis of accounting is appropriate in the circumstances but a material uncertainty exists, the auditor shall determine whether the financial statements:

- (a) Adequately disclose the principal events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and management's plans to deal with these events or conditions; and
- (b) Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

In such cases, the auditor shall express an unmodified opinion and the auditor's report shall include a separate section under the heading "Material Uncertainty Relating to Going Concern".

8.5.10. If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern but, based on the audit evidence obtained the auditor concludes that no material uncertainty exists, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework, the financial statements provide adequate disclosures about these events or conditions.

8.5.11. If the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud, the auditor shall evaluate the implications on the audit including on the assessed risks of material misstatement and the auditor's report.

8.6. Written Representations

[INZ] Written representations are necessary information that the auditor requests in connection with the audit of the entity's financial statements. Accordingly, similar to responses to einquiries, written representations are audit evidence. However, although written representations provide necessary audit evidence, they do not provide sufficient appropriate audit evidence on their own about any of the matters with which they deal. Furthermore, the fact that ~~management~~those charged with governance, or management, have~~has~~ provided reliable written representations does not affect the nature or extent of other audit evidence that the auditor obtains about the ~~fulfillment~~fulfilment of those charged with governance's, or management's, responsibilities, or about specific assertions.

²⁸ For the effect on the auditor's report see Part 9, paragraph 9.5.27.

²⁹ For the effect on the auditor's report see Part 9, paragraph 9.5.17.

³⁰ For the effect on the auditor's report see Part 9, paragraph 9.5.18.

[NZ] Written representations are requested from those responsible for the preparation of the financial statements. Those individuals may vary depending on the governance structure of the entity, and relevant law or regulation; however, those charged with governance (rather than management) are often the responsible party. In some circumstances, however, other parties, such as management, are also responsible for the preparation of the financial statements.

8.6.1. [Amended by the NZAuASB]

NZ8.6.1. The auditor shall obtain written representations from ~~management~~ those charged with governance who have appropriate knowledge of the matters concerned and responsibility for the financial statements, ~~and where appropriate those charged with governance,~~ about the following matters:

- (a) That they have fulfilled their responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation. The responsibilities shall be described in the same way in the representation as described in the terms of engagement;
- (b) That they have provided the auditor with all relevant information and access as agreed in the terms of the audit engagement;
- (c) That all transactions are recorded and are reflected in the financial statements;
- (d) That they acknowledge their responsibility for the design, implementation and maintenance of controls to prevent and detect fraud;
- (e) That they have disclosed to the auditor the result of its assessment of the risk that the financial statements may be materially misstated because of fraud;
- (f) That their knowledge of fraud, or suspected fraud, or allegations of fraud or suspected fraud has been disclosed to the auditor;
- (g) That they have disclosed to the auditor the identity of the entity's related parties and all the related party relationships and transactions of which they are aware;
- (h) That they have appropriately accounted for and disclosed related party relationships and transactions in accordance with the requirements of the financial reporting framework;
- (i) That all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements have been disclosed to the auditor;
- (j) That all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework;
- (k) With respect to accounting estimates, whether the methods, significant assumptions and data used in making the accounting estimates and disclosures are appropriate to achieve recognition, measurement or disclosure is in accordance with the applicable financial reporting framework;
- (l) That all events occurring subsequent to the date of the financial statements and for which the applicable financial reporting framework requires adjustment or disclosure have been adjusted or disclosed;
- (m) With respect to going concern, if a material uncertainty exists, information about their plans for future actions and the feasibility of these plans;

- (n) Regarding any restatement made to correct a material misstatement in prior period financial statements that affect the comparative information; and
- (o) Other representations the auditor determines necessary to support other audit evidence relevant to the financial statements or one or more specific assertions in the financial statements, including where necessary to support oral representations.

8.6.2. The auditor shall consider the need to obtain representations about specific accounting estimates.

8.6.3. The written representation shall be in the form of a representation letter addressed to the auditor.

Appendix 7 sets out an illustrative representation letter. If law or regulation requires management to make written public statements about its responsibilities, and the auditor determines that such statements provide some or all of the representations required by this standard, the relevant matters covered by such statements need not be included in the representation letter.

[NZ] If the auditor intends to rely on some, or all, of the written representations made by those charged with governance in a written public statement, the auditor ordinarily communicates their intention to place such reliance.

8.6.4. [Amended by the NZAuASB]

NZ8.6.4. The auditor shall request a written representation from ~~management, and where appropriate,~~ those charged with governance, whether they believe the effects of uncorrected misstatements are immaterial, individually or in aggregate, to the financial statements as a whole. A summary of such items shall be included in or attached to the written representation.

8.6.5. [Amended by the NZAuASB]

NZ8.6.5. —If the auditor has concerns about the competence, integrity, ethical values, or diligence of management or those charged with governance, or about its commitment to or enforcement of these, or representations received are inconsistent with other audit evidence, the auditor shall determine the effect on audit evidence more generally and take appropriate actions, including considering the possible effect on the opinion in the auditor's report³¹ having regard to the requirement in paragraph 8.6.7.

In the case of identified inconsistencies between one or more written representations and audit evidence obtained from another source, the auditor may consider whether the risk assessment remains appropriate and, if not, revise the risk assessment and determine the nature, timing and extent of further audit procedures to respond to the assessed risks.

[NZ] Concerns about the competence, integrity, ethical values or diligence of management or those charged with governance, or about its commitment to or enforcement of these, may cause the auditor to conclude that the risk of management misrepresentation in the financial statements is such that an audit cannot be conducted. In such a case, the auditor may consider withdrawing from the engagement, where withdrawal is possible under applicable law or regulation, unless those charged with governance put in place appropriate corrective measures. Such measures, however, may not be sufficient to enable the auditor to issue an unmodified audit opinion.

8.6.6. [Amended by the NZAuASB]

NZ8.6.6. —If management or those charged with governance does not provide one or more of the requested written representations, the auditor shall:

- (a) Discuss the matter with management;

³¹ For the effect on the auditor's report see Part 9, paragraph 9.5.22.

- (b) Re-evaluate the integrity of management and evaluate the effect this may have on the reliability of oral and written representations and audit evidence in general; and
- (c) Take appropriate actions, including determining the possible effect on the opinion in the auditor's report³² having regard to the requirement in paragraph 8.6.7.

8.6.7. [Amended by the NZAuASB]

NZ8.6.7. —If the auditor concludes that there is sufficient doubt about the integrity of **management those charged with governance** such that the written representations required by paragraphs 8.6.1.(a)–(c) are not reliable³³ or management does not provide the written representations required by paragraphs 8.6.1.(a)–(c),³⁴ the auditor shall disclaim an opinion on the financial statements.

8.6.8. The date of the written representations shall be as near as practicable to, but not after, the date of the auditor's report on the financial statements. The written representations shall be for all financial statements and period(s) referred to in the auditor's report.

8.7. Taking Overall Responsibility for Managing and Achieving Quality

8.7.1. Prior to dating the auditor's report, the engagement partner shall determine that the engagement partner has taken overall responsibility for managing and achieving quality on the audit engagement. In doing so, the engagement partner shall determine that:

- (a) The engagement partner's involvement has been sufficient and appropriate throughout the audit engagement such that the engagement partner has the basis for determining that the significant **judgmentjudgements** made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement; and
- (b) The nature and circumstances of the audit engagement, any changes thereto, and the firm's related policies or procedures have been taken into account.

8.7.2. On or before the date of the auditor's report, the engagement partner shall determine that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor's report to be issued.

8.7.3. Prior to dating the auditor's report, the engagement partner shall review the financial statements and the auditor's report to determine that the report to be issued is appropriate in the circumstances.

8.8. Specific Communication Requirements

8.8.1. The auditor shall communicate, on a timely basis, all misstatements accumulated during the audit with the appropriate level of management, unless prohibited by law or regulation.

8.8.2. The auditor shall communicate with those charged with governance:

- (a) Uncorrected misstatements and the effect that they, individually or in aggregate, may have on the auditor's opinion, unless prohibited by law or regulation. The auditor's communication shall identify the material uncorrected misstatements individually.
- (b) The effect of uncorrected misstatements from prior periods on the current year's financial statements.

³² For the effect on the auditor's report see Part 9, paragraph 9.5.23.

³³ For the effect on the auditor's report see Part 9, paragraph 9.5.24.

³⁴ For the effect on the auditor's report see Part 9, paragraph 9.5.25.

- (c) The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates, and financial statement disclosures.
- (d) Significant difficulties, if any, encountered during the audit.
- (e) Significant matters arising during the audit, including in connection to the entity's related parties, that were discussed, or subject to correspondence, with management.
- (f) Significant findings from the audit. If, in the auditor's professional ~~judgment~~judgement, oral communications would not be adequate this communication shall be in writing.
- (g) Other matters not already reported related to fraud that may be relevant to the responsibilities of those charged with governance, unless prohibited by law or regulation.
- (h) Circumstances, if any, that affect the form and content of the auditor's report.
- (i) Written representations the auditor is requesting.
- (j) Other significant matters, if any, arising from the audit that, in the auditor's professional ~~judgment~~judgement, are relevant to the oversight of the financial reporting process.
- (k) The expectation thereof and the wording if the auditor expects to include an Emphasis of Matter or Other Matter Paragraph in the auditor's report.

8.8.3. Unless all those charged with governance are involved in managing the entity, the auditor shall communicate with those charged with governance events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:

- (a) Whether the events or conditions constitute a material uncertainty;
- (b) Whether management's use of the going concern basis of accounting is appropriate in the preparation of the financial statements;
- (c) The adequacy of related disclosures in the financial statements; and
- (d) Where applicable, the implications for the auditor's report.

8.9. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

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.

PES 3/SQM 1 (or national requirements that are at least as demanding) requires firms' systems of quality management to establish a quality objective that addresses the assembly of

engagement documentation on a timely basis after the date of the engagement reports.³⁵ An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report.³⁶

- 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.

~~PES 3/SQM 1~~ (or national requirements that are at least as demanding) requires firms' systems of quality management to establish a quality objective to address the appropriate maintenance and retention of engagement documentation to meet the needs of the firm and to comply with law, regulation, relevant ethical requirements, or professional standards.³⁷ The retention period for audit engagements ordinarily is no shorter than five years from the date of the auditor's report, or, if later, the date of the auditor's report on the group financial statements, when applicable.³⁸

- 8.9.5. If applicable, the auditor shall document the failure to meet an objective of any Part of the ~~ISA for LCE~~ ISA (NZ) 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.

³⁵ PES 3, paragraph 31(f)

³⁶ PES 3, paragraph A83

³⁷ PES 3, paragraph 31(f)

³⁸ PES 3, paragraph A85

9. Forming an Opinion and Reporting

Content of this Part

Part 9 sets out the requirements for:

- Forming an opinion;
- The types of audit opinions; and
- The content of the auditor's report.
- Other Information and Comparative Information.

Scope of this Part

This Part explains the content of the auditor's report and sets out the auditor's determination of modifications to the opinion, as well as when other amendments to the auditor's report are needed. It also sets out the auditor's required procedures in relation to corresponding figures and comparative financial statements, and other information (if applicable).

Examples of modified opinions, a material uncertainty related to going concern, emphasis of matter and other matter paragraphs, and related guidance on auditor reports, can be found in the *Auditor Reporting Supplemental Guide*.

9.1. Objectives

9.1.1. The objectives of the auditor are to:

- (a) Form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained and to express clearly that opinion through a written report; and
- (b) Consider whether there is a material inconsistency between the other information, if any, and the:
 - (i) Financial statements; and
 - (ii) Auditor's knowledge obtained in the audit.

9.2. Forming an Opinion on the Financial Statements

9.2.1. The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

9.2.2. In order to form that opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. That conclusion shall take into account:

- (a) Whether sufficient appropriate audit evidence has been obtained;
- (b) Whether uncorrected misstatements are material, individually or in aggregate; and
- (c) The evaluations required by paragraphs 9.2.3. to 9.2.6.

9.2.3. The auditor shall evaluate whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework. This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's ~~judgment~~judgements.

9.2.4. In performing the evaluation in paragraph 9.2.3., the auditor shall evaluate, in view of the requirements of the applicable financial reporting framework, whether:

- (a) The financial statements appropriately disclose the entity's significant accounting policies, and whether they have been presented in an understandable way;
- (b) The entity's accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;
- (c) The accounting estimates and related disclosures made by management are reasonable;
- (d) The identified related party relationships and transactions have been appropriately accounted for, presented and disclosed in accordance with the applicable financial reporting framework;
- (e) The information presented in the financial statements is relevant, reliable, comparable and understandable including whether:
 - (i) The information that should have been included has been included;
 - (ii) Such information is appropriately classified, aggregated or disaggregated, and characterized; and
 - (iii) The overall presentation of the financial statements has been undermined by including information that is not relevant or that obscures a proper understanding of the matters disclosed;
- (f) The financial statements provide adequate disclosures to enable intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and
- (g) The terminology used in the financial statements, including the title of each financial statement, is appropriate.

9.2.5. When the financial statements are prepared in accordance with a fair presentation framework, the auditor shall also evaluate whether the financial statements achieve fair presentation. This evaluation shall include consideration of:

- (a) The overall presentation, structure and content of the financial statements; and
- (b) Whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The auditor's evaluation about whether the financial statements achieve fair presentation, both in respect of presentation and the disclosures necessary to achieve it, is a matter of professional judgment.

9.2.6. The auditor shall evaluate whether the financial statements adequately refer to or describe the applicable financial reporting framework.

9.3. Form of Opinion

9.3.1. The auditor shall express an unmodified opinion when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

If the financial reporting framework is a fair presentation framework, as is generally the case for general purpose financial statements, the opinion required is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view. If the financial reporting framework is a compliance framework, the opinion required is on whether the financial statements are prepared, in all material respects, in accordance with the framework.

9.3.2. If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor shall discuss the matter with management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, determine whether to modify the opinion.³⁹

9.3.3. If the financial statements are prepared in accordance with a compliance framework, the auditor is not required to evaluate whether the financial statements achieve fair presentation. However, if in extremely rare circumstances the auditor concludes, based on the audit evidence obtained, that such financial statements are misleading, the auditor shall discuss the matter with management and, depending on how it is resolved, shall determine whether, and how, to communicate it in the auditor's report.⁴⁰

9.4. Auditor's Report

9.4.1. [Amended by the NZAuASB]

NZ9.4.1. The auditor shall report in accordance with the specified format and content below unless:

- (a) Amendment to the auditor's report is required for compliance with a specific layout or wording of the auditor's report required by law or regulation of a jurisdiction or in the Auditor-General's Auditing Standards. When the layout or wording of the auditor's report is prescribed by law or regulation or in the Auditor-General's Auditing Standards, the auditor's report shall refer to this ~~ISA for LCE~~ ISA (NZ) for LCE only if the elements of the specified format and content illustrated below are included; or
- ~~(b) The auditor is required to conduct the audit in accordance with the auditing standard of a specific jurisdiction for less complex entities (the "national LCE auditing standard") that prescribes a layout or wording of the auditor's report different from that required by the ISA for LCE and has additionally complied with the ISA for LCE in the conduct of the audit. If this is the case, the auditor's report may refer to the ISA for LCE in addition to the national LCE auditing standard only if the auditor's report includes the elements of the specified format and content illustrated below; or~~
- ~~(be) —~~The auditor's report includes a modified opinion, emphasis of matter paragraph, other matter paragraph, material uncertainty related to going concern, other reporting responsibilities, or a separate section dealing with Other Information, in which case the auditor shall modify the auditor's opinion (according to Part 9.5.) or amend the auditor's report (according to Part 9.8.).

NZ9.4.1.A. An auditor, when applying this standard, is required to conduct an audit in accordance with the ISA (NZ) for LCE. Compliance with the ISA (NZ) for LCE will also mean the auditor has complied with the ISA for LCE in the conduct of the audit. In this case, the auditor's report may refer to the ISA for LCE in addition to the ISA (NZ) for LCE only if the auditor's report includes the elements of the specified format and content illustrated below.

INDEPENDENT AUDITOR'S REPORT

To the [Shareholders of ABC Company or Other Appropriate Addressee]⁴¹

Opinion

We have audited⁴² the financial statements of [ABC Company (the Entity)], which comprise the statement of financial position as at December 31, 20X~~X~~4, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies (replace these report names with the appropriate titles)].⁴³

In our opinion, the accompanying financial statements ["present fairly, in all material respects" or "give a true and fair view of"]⁴⁴ the financial position of the [Entity] as at [December 31, 20X~~X~~4], and [of] its financial performance and its cash flows for the year then ended in accordance with [applicable financial reporting framework] issued by the New Zealand Accounting Standards Board.⁴⁵

Basis for Opinion

We conducted our audit in accordance with the International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (the ~~ISA for LCE~~ ISA (NZ) for LCE). Our responsibilities under the ~~ISA for LCE~~ ISA (NZ) for LCE are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.⁴⁶ We are independent of the [Entity] in accordance with Professional and Ethical Standard 1 International Code of Ethics for Assurance Practitioners (including International Independence Standards (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board, ~~the ethical requirements that are relevant to our audit of the financial statements in [jurisdiction]~~, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.⁴⁷

Other than in our capacity as auditor we have no relationship with, or interests in, the [Entity].⁴⁸

Responsibilities of [~~Management~~ Those Charged with Governance] for the Financial Statements⁴⁹

~~[Management]~~ Those Charged with Governance ~~are~~ is responsible on behalf of the [Entity] for the preparation [and fair presentation] of the financial statements in accordance with [applicable financial reporting framework],⁵⁰ and for such internal control as [~~management~~ Those Charged with Governance] determines ~~is~~ necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, [~~Those Charged with Governance~~ management] ~~is~~ are responsible for assessing the [Entity's] ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless [~~management~~ Those Charged with Governance] either intends to liquidate the [Entity] or to cease operations, or ~~has~~ have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements^{51 52}

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ~~ISA for LCE~~ ISA (NZ) for LCE will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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- ⁴¹ Matters reflected in the specified format and content of the auditor's report in square brackets (e.g. []) are to be tailored accordingly.
- ⁴² When disclaiming an opinion, the statement which indicates that the financial statements have been audited is amended to state that the auditor was engaged to audit the financial statements.
- ⁴³ Identify the entity whose financial statements have been audited; identify each financial statement and its date and period, and refer to the notes and significant accounting policies or use another appropriate description in accordance with the applicable financial reporting framework.
- ⁴⁴ See also 9.4.2. below. When the financial statements are prepared in accordance with a compliance framework, the opinion and description of the auditor's responsibilities refer instead to whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.
- ⁴⁵ [NZ] Identify the jurisdiction of origin of the financial reporting framework if it is not International Financial Reporting Standards or International Public Sector Accounting Standards as issued by the International Public Sector Accounting Standards Board. For an entity in New Zealand, that is required to apply the New Zealand Accounting Standards Framework, the reference to the applicable financial reporting framework in the auditor's opinion should be to the applicable financial reporting requirements issued by the New Zealand Accounting Standards Board of the External Reporting Board that apply to the tier under which the entity is reporting.
- ⁴⁶ When the auditor disclaims an opinion on the financial statements, this statement is not included in the auditor's report.
- ⁴⁷ When the auditor expresses a qualified or adverse opinion, the statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion is amended to include the word "qualified" or "adverse", as appropriate. When the auditor disclaims an opinion on the financial statements, this statement is not included in the auditor's report.
- ⁴⁸ [NZ] If the auditor has any relationship (other than that of auditor) with, or any interests in, the entity, then this statement is amended.
- ⁴⁹ [NZ] Or other terms that are appropriate in the context of the legal framework of the particular jurisdiction. In New Zealand, the appropriate reference is usually to those charged with governance. In some jurisdictions, the appropriate reference may be to management.
- ⁵⁰ [NZ] Where Those Charged with Governance's responsibility is to prepare financial statements that give a true and fair view, this may read: "Those Charged with Governance are responsible for the preparation of financial statements that give a true and fair view in accordance with [applicable financial reporting framework], and for such ..."
- ⁵¹ [NZ] The description of the auditor's responsibilities may also be included within an appendix, or refer to a description to the relevant page of the auditors responsibilities on the External Reporting Board's website at <https://www.xrb.govt.nz/standards/assurance-standards/auditors-responsibilities/>. The auditor shall determine that such a description is not inconsistent with this ISA (NZ) for LCE. In such cases, a reference to the location of appendix or description shall be included within the auditor's report, accompanied by "This description forms part of our auditor's report". When the auditor disclaims an opinion on the financial statements, the description of the auditor's responsibilities only includes the matters required by paragraph 9.5.33.
- ⁵² When Part 10 applies, further describe the auditor's responsibilities in a group audit engagement by stating that;
- (i) The auditor's responsibilities are to plan and perform the group audit to obtain sufficient appropriate audit evidence regarding the financial information of the entities or business units within the group as a basis for forming an opinion on the group financial statements;
 - (ii) The auditor is responsible for the direction, supervision and review of the audit work performed for purposes of the group audit; and
 - (iii) The auditor remains solely responsible for the auditor's opinion.

As part of an audit in accordance with the ~~ISA for LCE~~ISA (NZ) for LCE, we exercise professional ~~judgment~~judgement and maintain professional ~~skepticism~~scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the [Entity's] internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by [management and Those Charged with Governance].
- Conclude on the appropriateness of ~~management's~~Those Charged with Governance's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the [Entity's] ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the [Entity] to cease to continue as a going concern.
- [Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.]⁵³

We communicate with [management, and where appropriate, those charged with governance] regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

[Signature in the name of the audit firm⁵⁴, ~~the personal name of the auditor, or both, as appropriate for the particular jurisdiction~~]

[Auditor Address: name the location in the jurisdiction where the auditor practices]

[Date: No earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements, including evidence that (i) All the statements and disclosures that comprise the financial statements have been prepared; and (ii) Those with the ~~recognized~~recognised authority have asserted that they have taken responsibility for those financial statements.]

9.4.2. When the financial statements are prepared in accordance with a fair presentation framework, the auditor shall refer to "the preparation and fair presentation of these financial statements" or "the preparation of financial statements that give a true and fair view," as appropriate in the circumstances, in the description of responsibilities for the financial statements in the auditor's report.

9.4.3. The auditor shall not refer to the work of an auditor's expert in an auditor's report containing an unmodified opinion unless required by law or regulation to do so. If such reference is required by

⁵³ Relevant when the financial statements are prepared in accordance with a fair presentation framework.

⁵⁴ [NZ] Law or regulation may require that the auditors' report include the name of the engagement partner responsible for audits. The auditor may be required by law or regulation, or may decide, to include additional information beyond the engagement partner's name in the auditor's report to further identify the engagement partner, for example, the engagement partner's professional license number that is relevant to where the auditor practices.

law or regulation, the auditor shall indicate in the auditor's report that the reference does not reduce the auditor's responsibility for the auditor's opinion.

9.5. Modifications to the Opinion

Tables A to C below set out the requirements for which a modified opinion is to be used in different situations, and the form and content of a modified opinion.

9.5.1. The auditor shall modify the opinion in the auditor's report according to Tables A–C below when:

- (a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or
- (b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

9.5.2. When the auditor modifies the audit opinion, the auditor shall:

- (a) Amend the heading "Basis for Opinion" to "Basis for Qualified Opinion," "Basis for Adverse Opinion," or "Basis for Disclaimer of Opinion" as set out in Tables A–C; and
- (b) Within the basis for opinion section, include a description of the matter giving rise to the modification.

Table A below specifies how the auditor's professional ~~judgment~~ judgement about the nature of the matter giving rise to the modification, and the pervasiveness of its effects or possible effects on the financial statements, affects the type of opinion to be expressed.

TABLE A Nature of Matter Giving Rise to the Modification	Auditor's Professional Judgment Judgement about the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but Not Pervasive	Material and Pervasive
<i>Financial statements are materially misstated</i>	Qualified opinion	Adverse opinion
<i>Inability to obtain sufficient appropriate audit evidence</i>	Qualified opinion	Disclaimer of opinion

Table B below specifies the modification to be made to the opinion for each type of opinion in Table A.

TABLE B Form of opinion	Fair Presentation Framework	Compliance Framework
9.5.3. Qualified opinion Auditor's Report – Heading for opinion: "Qualified Opinion"	"In our opinion, except for the [effects or possible effects] ⁵⁵ of the matter(s) described in the Basis for Qualified Opinion section, the accompanying	"...except for the [effects or possible effects] of the matter(s) described in the Basis for Qualified Opinion section, the accompanying financial

⁵⁵ Matters reflected in square brackets (e.g., []) are to be tailored accordingly

Auditor's Report – Heading for Basis for Opinion: “Basis for Qualified Opinion”	financial statements [present fairly, in all material respects / [give a true and fair view of] [...] in accordance with [the applicable financial reporting framework]”	statements have been prepared, in all material respects, in accordance with [the applicable financial reporting framework]”
9.5.4. Adverse opinion Auditor's Report – Heading for opinion: “Adverse Opinion” Auditor's Report – Heading for Basis for Opinion: “Basis for Adverse Opinion”	“...the accompanying financial statements do not [present fairly /give a true and fair view of] [...] in accordance with [the applicable financial reporting framework]”	“...the accompanying financial statements have not been prepared, in all material respects, in accordance with [the applicable financial reporting framework]”
9.5.5. Disclaimer of opinion Auditor's Report – Heading for opinion: “Disclaimer of Opinion” Auditor's Report – Heading for Basis for Opinion: “Basis for Disclaimer of Opinion”	<p>“We were engaged to audit the financial statements of...”</p> <p>“We do not express an opinion on the accompanying financial statements.</p> <p>Because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements.”</p>	

Table C below sets out specific circumstances when the auditor's opinion is to be modified, and the types of opinions expressed in those circumstances based on the nature of the matter giving rise to the modification (see Table A). Table C is not an exhaustive list of all circumstances when the auditor's opinion is to be modified.

TABLE C				
Specific Circumstances When the Auditor's Opinion is to be Modified	Para Ref	Qualified	Adverse	Disclaimer
<i>Opening Balances</i>				
9.5.6. The auditor is unable to obtain sufficient appropriate audit evidence regarding the opening balances.	4.5.4.	✓		✓
9.5.7. The auditor concludes, based on the audit evidence obtained, that the opening balances contain a misstatement that materially affects the current period's financial statements, and the effect of the misstatement is not appropriately	4.5.5.	✓	✓	

TABLE C				
Specific Circumstances When the Auditor's Opinion is to be Modified	Para Ref	Qualified	Adverse	Disclaimer
accounted for or not adequately presented or disclosed.				
9.5.8. The auditor concludes, based on the audit evidence obtained, that the current period's accounting policies are not consistently applied in relation to opening balances in accordance with the applicable financial reporting framework or a change in accounting policies is not appropriately accounted for or adequately presented or disclosed, in accordance with the financial reporting framework.	4.5.6.	✓	✓	
9.5.9. The predecessor auditor's opinion regarding the prior period's financial statements included a modification that remains relevant and material to the current period's financial statements.	4.5.3.	✓	✓	✓
<i>Non-Compliance with Laws and Regulations</i>				
9.5.10. Sufficient information about suspected non-compliance cannot be obtained.	7.4.26.	✓		✓
9.5.11. The auditor concludes that the identified or suspected non-compliance has a material effect on the financial statements and has not been adequately reflected in the financial statements.	7.4.27.	✓	✓	
9.5.12. The auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial statements has, or is likely to have, occurred.	7.4.27.	✓		✓
9.5.13. The auditor is unable to determine whether non-compliance has occurred because of limitations	7.4.27.	✓		✓

TABLE C				
Specific Circumstances When the Auditor's Opinion is to be Modified	Para Ref	Qualified	Adverse	Disclaimer
imposed by the circumstances rather than by management or those charged with governance.				
<i>External Confirmations</i>				
9.5.14. The auditor concludes that management's refusal to allow the auditor to send a confirmation request is unreasonable, or the auditor is unable to obtain relevant and reliable audit evidence from alternative audit procedures.	7.3.24.	✓		✓
<i>Inventory</i>				
9.5.15. The auditor cannot perform alternative audit procedures to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory.	7.4.21.	✓		✓
<i>Litigation and Claims</i>				
9.5.16. Management refuses to give the auditor permission to communicate or meet with the entity's external legal counsel, or the entity's external legal counsel refuses to respond appropriately to the letter of <u>e</u> inquiry, or is prohibited from responding; and the auditor is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures.	7.4.25.	✓		✓
<i>Going Concern</i>				
9.5.17. The financial statements have been prepared using the going concern basis of accounting but, in the auditor's professional judgment <u>judgement</u> , management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate.	7.4.1. 8.5.7.		✓	

TABLE C Specific Circumstances When the Auditor's Opinion is to be Modified	Para Ref	Qualified	Adverse	Disclaimer
<p>9.5.18. Adequate disclosures are not made about a material uncertainty in the financial statements.</p> <p>9.5.19. In this circumstance, the basis for qualified (or adverse) opinion section shall state that "a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter."</p>	<p>7.4.4. 8.5.8.</p>	<p>✓</p>	<p>✓</p>	
<p><u>9.5.20. [Amended by the NZAuASB]</u></p> <p><u>NZ</u>9.5.20. When evaluating management's assessment of the entity's ability to continue as a going concern, the period is less than twelve months from the date of the financial auditor's current report statements, and management does not make or extend its assessment, leading to the auditor being unable to obtain sufficient appropriate audit evidence.</p>	<p>7.4.2.</p>	<p>✓</p>		<p>✓</p>
<i>Subsequent Events</i>				
<p>9.5.21. Facts become known to the auditor after the date of the auditor's report but before the date the financial statements are issued, and management does not amend the financial statements in circumstances where the auditor believes they need to be amended.</p>	<p>8.4.6.</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>
<i>Written Representations</i>				
<p>9.5.22. The auditor concludes that the written representations required by this standard are not reliable.</p>	<p>8.6.5.</p>	<p>✓</p>		<p>✓</p>
<p>9.5.23. Management does not provide one or more of the requested written representations.</p>	<p>8.6.6.</p>	<p>✓</p>		<p>✓</p>

TABLE C				
Specific Circumstances When the Auditor's Opinion is to be Modified	Para Ref	Qualified	Adverse	Disclaimer
9.5.24. The auditor concludes that there is sufficient doubt about the integrity of management such that the written representations required by 8.6.1.(a)–(c) are not reliable.	8.6.7.			✓
9.5.25. When management does not provide the written representations required by paragraphs 8.6.1.(a)–(c).	8.6.7.			✓
<i>Corresponding Figures</i>				
9.5.26. Corresponding figures are presented, the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modification is unresolved. The Basis for Modification paragraph shall either: (a) refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material,; or (b) in other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.	9.7.6.	✓	✓	✓
<i>Other Items</i>				
9.5.27. The auditor is unable to obtain sufficient appropriate audit evidence.	8.5.6.	✓		✓
9.5.28. The financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation.	9.3.2.		✓	

TABLE C Specific Circumstances When the Auditor's Opinion is to be Modified	Para Ref	Qualified	Adverse	Disclaimer
9.5.29. The financial statements are prepared in accordance with a compliance framework and, in extremely rare circumstances, the auditor concludes, based on the audit evidence obtained, that such financial statements are misleading.	9.3.3.	✓	✓	✓

Other Matters Relating to Modifications

9.5.30. If the auditor makes reference to the work of an auditor's expert in the auditor's report because such reference is relevant to an understanding of a modification to the auditor's opinion, the auditor shall indicate in the auditor's report that such reference does not reduce the auditor's responsibility for that opinion.

9.5.31. If there is a material misstatement of the financial statements that relates to:

- (a) Specific amounts in the financial statements (including quantitative disclosures), the auditor shall include in the Basis for Opinion section a description and quantification of the financial effects of the misstatement, unless impracticable. If it is not practicable to quantify the financial effects, the auditor shall so state in this section.
- (b) Qualitative disclosures, the auditor shall include in the Basis for Opinion section an explanation of how the disclosures are misstated.
- (c) The non-disclosure in the financial statements of information required to be disclosed, the auditor shall:
 - (i) Discuss the non-disclosure with those charged with governance;
 - (ii) Describe in the Basis for Opinion section the nature of the omitted information; and
 - (iii) Unless prohibited by law or regulation, include the omitted disclosures, provided it is practicable to do so and the auditor has obtained sufficient appropriate audit evidence about the omitted information.

9.5.32. If the modification results from an inability to obtain sufficient appropriate audit evidence, the auditor shall include in the Basis for Opinion section the reasons for that inability.

9.5.33. When the auditor disclaims an opinion on the financial statements due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the Auditor's Responsibilities for the Audit of the Financial Statements section of the report under paragraph 9.4.1. to include only the following:

- (a) A statement that the auditor's responsibility is to conduct an audit of the entity's financial statements in accordance with the ~~ISA for LCE~~ [ISA \(NZ\) for LCE](#) and to issue an auditor's report;
- (b) A statement that because of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and

- (c) A statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements.

(NZ d) In New Zealand, the statement required by paragraph 9.5.33.(c) shall refer to Professional and Ethical Standard 1 International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board.

9.5.34. If the auditor has expressed an adverse opinion or disclaimed an opinion on the financial statements, the auditor shall describe in the Basis for Opinion section the reasons for any other matters of which the auditor is aware that would have required a modification to the opinion, and the effects thereof.

9.6. Other Paragraphs in the Auditor's Report

Emphasis of Matter paragraphs and Other Matter paragraphs in the auditor's report are used when the auditor considers it necessary to:

- *Draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements (Emphasis of Matter); or*
- *Draw users' attention to any matter or matters other than those presented or disclosed in the financial statements that are relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report (Other Matter).*

Emphasis of Matter Paragraphs

9.6.1. If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's professional ~~judgment~~judgement, is of such importance that it is fundamental to the users' understanding of the financial statements, and the auditor would not be required to modify the opinion as a result of that matter, the auditor shall include an Emphasis of Matter paragraph in the auditor's report indicating that the auditor's report is not modified in respect of the matter ~~emphasized~~emphasised.

Examples of where Emphasis of Matter paragraphs may be needed include:

- *When a financial reporting framework prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation.*
- *When facts become known to the auditor after the date of the auditor's report and the auditor provides a new or amended auditor's report (i.e., subsequent events).*

The inclusion of an Emphasis of Matter paragraph in the auditor's report does not affect the auditor's opinion. An Emphasis of Matter paragraph is not a substitute for:

- *A modified opinion when required by the circumstances of a specific audit engagement;*
- *Disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation; or*
- *Reporting when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern.*

Other Matter Paragraphs

The content of an Other Matter paragraph reflects clearly that such other matter is not required to be presented and disclosed in the financial statements. An Other Matter paragraph does not include information that the auditor is prohibited from providing by law, regulation or other professional standards, for example, ethical standards for the confidentiality of information. An Other Matter paragraph also does not include information that is required to be provided by management.

9.6.2. If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor's professional ~~judgment~~judgement, is relevant to the users' understanding of the audit, the auditor's responsibilities or the auditor's report the auditor shall include an Other Matter paragraph in the auditor's report provided this is not prohibited by law or regulation.

Content of Other Paragraphs in the Audit Report

9.6.3. When the auditor includes an Emphasis of Matter, Other Matter paragraph or a material uncertainty related to going concern in the auditor's report, the auditor shall include the paragraph or section according to Table D below:

TABLE D Paragraph or Section	Location	Heading shall include	Content shall include
9.6.4. Emphasis of Matter paragraph	A separate section of the auditor's report	Appropriate heading that includes "Emphasis of Matter"	A clear reference to the matter being emphasized <u>emphasised</u> and to where relevant disclosures that fully describe the matter can be found in the financial statements. A reference only to information presented or disclosed in the financial statements. An indication that the auditor's opinion is not modified in respect of the matter emphasized <u>emphasised</u> .
9.6.5. Other Matter paragraph	A separate section of the auditor's report	Appropriate heading that includes "Other Matter"	As appropriate in the circumstances.
9.6.6. Material Uncertainty Related to Going Concern paragraph	A separate section of the auditor's report	"Material Uncertainty Related to Going Concern"	Draw attention to the note in the financial statements that discloses the matters related to the material uncertainty. State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the auditor's opinion is not modified in respect of the matter.

9.6.7. When facts become known to the auditor after the financial statements have been issued and if management amends the financial statements, the auditor shall include in the new or amended auditor's report an Emphasis of Matter paragraph or Other Matter paragraph drawing users'

attention to the reason for the amendment and referring to the earlier report provided by the auditor.

9.7. Comparative Information – Corresponding Figures and Comparative Financial Statements

[NZ] In New Zealand, the auditor's opinion on financial statements prepared under New Zealand generally accepted accounting practice refers to financial statements for the current period, which include corresponding figures, and not to comparative financial statements. Consequently, paragraphs 9.7.1., 9.7.2., 9.7.4., 9.7.7. and 9.7.8. have no application.

9.7.1. The auditor shall determine whether the financial statements include the comparative information required by the applicable financial reporting framework and whether such information is appropriately classified. In doing so, the auditor shall evaluate whether:

- (a) The amounts and disclosures in the prior period agree with comparative information or have been restated; and
- (b) The accounting policies reflected in the comparative information are consistent with those applied in the current period or, where changes occurred, have been properly accounted for and adequately presented or disclosed.

9.7.2. If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists. If the prior period financial statements are amended, the auditor shall determine that the comparative information agrees with the amended financial statements.

9.7.3. If the financial statements of the prior period were audited by a predecessor auditor and the auditor is not prohibited by law or regulation from referring to the predecessor auditor's report on the corresponding figures and decides to do so, the auditor shall state in an Other Matter paragraph in the auditor's report:

- (a) That the financial statements of the prior period were audited by a predecessor auditor;
- (b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefore; and
- (c) The date of that report.

9.7.4. If the financial statements of the prior period were audited by a predecessor auditor and are presented as comparative financial statements, in addition to expressing an opinion on the current period's financial statements, the auditor shall state in an Other Matter paragraph:

- (a) That the financial statements of the prior period were audited by a predecessor auditor;
- (b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefore; and
- (c) The date of that report, unless the predecessor auditor's report on the prior period's financial statements is reissued with the financial statements.

9.7.5. If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph in the auditor's report that the corresponding figures or comparative financial statements are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.

Corresponding Figures

9.7.6. When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in accordance with paragraph 9.7.5. or in the following circumstances:

- (a) If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modification is unresolved, the auditor shall modify the auditor's opinion on the current period's financial statements.⁵⁶
- (b) If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion has been previously issued, and the corresponding figures have not been properly restated or appropriate disclosures have not been made, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.

Comparative Financial Statements

9.7.7. When comparative financial statements are presented, the auditor's opinion shall refer to each period for which financial statements are presented and on which an audit opinion is expressed.

9.7.8. When reporting on prior period financial statements in connection with the current period's audit, if the auditor's opinion on such prior period financial statements differs from the opinion the auditor previously expressed, the auditor shall disclose the substantive reasons for the different opinion in an Other Matter paragraph.

9.8. Other Information

"Other information" is financial or non-financial information (other than the financial statements and the auditor's report thereon) included in an entity's annual report.

9.8.1. The auditor shall determine, through discussion with management, which document(s) comprises the annual report, and the entity's planned manner and timing of the issuance of such document(s).

9.8.2. The auditor shall read the other information, and:

- (a) Consider whether there is a material inconsistency between the other information and the financial statements; and
- (b) Consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained in the audit.

9.8.3. As the basis for the considerations in paragraph 9.8.2.(a), the auditor shall, to evaluate their consistency, compare selected amounts or other items in the other information (that are intended to be the same as, to ~~summarize~~summarise, or to provide greater detail about, the amounts or other items in the financial statements) with such amounts or other items in the financial statements.

In evaluating the consistency of selected amounts or other items, the auditor is not required to compare all amounts or other items in the other information that are intended to be the same as, or ~~summarize~~summarise, or to provide greater details about, the amounts or other items within the financial statements, with such amounts or other items in the financial statements.

⁵⁶ For the effect on the auditor's report see Part 9, paragraph 9.5.26.

- 9.8.4. While reading the other information, the auditor shall also remain alert for indications that the remainder of the other information, which is unrelated to the financial statements or the auditor's knowledge obtained in the audit, appears to be materially misstated.
- 9.8.5. If the auditor identifies that a material inconsistency appears to exist (or becomes aware that the other information appears to be materially misstated), the auditor shall discuss the matter with management and, if necessary, perform other procedures to conclude whether:
- A material misstatement of the other information exists;
 - A material misstatement of the financial statements exists; or
 - The auditor's understanding of the entity and its environment needs to be updated.
- 9.8.6. If the auditor concludes, based on the audit evidence obtained, that a material misstatement of the other information exists, the auditor shall request management to correct the other information. If management:
- Agrees to make the correction, the auditor shall determine that the correction has been made; or
 - Refuses to make the correction, the auditor shall communicate the matter with those charged with governance and request that the correction be made. If the correction is still not made, the auditor shall consider the implications for the auditor's report in accordance with Table E below or withdraw from the engagement where this is possible.
- 9.8.7. If the auditor obtained some, or all of, the other information at the date of the auditor's report, the auditor shall include an Other Information section in the auditor's report in accordance with Table E.

TABLE E Paragraph or Section	Location	Heading shall include	Content shall include
<p>9.8.8. [Amended by the NZAuASB]</p> <p>NZ9.8.8. — Other Information Section</p>	A separate section of the auditor's report	"Other Information" or other appropriate title	<ol style="list-style-type: none"> A statement that management those charged with governance is responsible for the other information; An identification of the other information, if any, obtained by the auditor prior to the date of the auditor's report; A statement that the auditor's opinion does not cover the other information and, accordingly, that the auditor does not express an audit opinion or any form of assurance conclusion thereon; A description of the auditor's responsibilities relating to reading, considering and reporting on other information as required by this ISA for LCE ISA (NZ) for LCE; and When other information has been obtained prior to the date of the auditor's report, either: <ol style="list-style-type: none"> A statement that the auditor has nothing to report; or

			(ii) If the auditor has concluded that there is an uncorrected material misstatement of the other information, a statement that describes the uncorrected material misstatement of the other information.
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9.8.9. Unless required by law or regulation, when the auditor disclaims an opinion on the financial statements, the auditor's report shall not include an Other Information section.

9.9. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

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

Content of this Part

Part 10 sets out the special considerations that apply to a group audit. Throughout this Part, “the auditor” should be read as the “group auditor”.

Scope of this Part

All Parts of the ~~ISA for LCE~~ ISA (NZ) for LCE apply to a group audit. The requirements and guidance in this Part refer to, or expand on, the application of other Parts of the ~~ISA for LCE~~ ISA (NZ) for LCE to a group audit.

10.1. Objective

10.1.1. The objective of the auditor is to identify and assess the risks of material misstatement of the group financial statements, whether due to fraud or error, and plan and perform further audit procedures to appropriately respond to those assessed risks.

10.2. Planning Activities

10.2.1. In applying Part 5, the auditor shall establish, and update as necessary, the scope, timing and direction of the group audit. In doing so, the auditor shall determine:

- (a) The components at which audit work will be performed; and
- (b) The resources needed to perform the group audit engagement.

Components

The determination of components at which to perform audit work is a matter of professional ~~judgment~~ judgement. Matters that may influence the auditor’s determination include, for example:

- *The nature of events or conditions that may give rise to risks of material misstatement at the assertion level of the group financial statements that are associated with a component, for example, newly formed or acquired entities or business units or entities or business units in which significant changes have taken place.*
- *The disaggregation of significant classes of transactions, account balances and disclosures in the group financial statements across components, considering the size and nature of assets, liabilities and transactions at the location or business unit relative to the group financial statements.*
- *Whether sufficient appropriate audit evidence is expected to be obtained for all significant classes of transactions, account balances and disclosures in the group financial statements from audit work planned on the financial information of identified components.*
- *The nature and extent of misstatements or control deficiencies identified at a component in prior period audits.*
- *The nature and extent of the commonality of controls across the group and whether, and if so, how, the group ~~centralizes~~ centralises activities relevant to financial reporting.*

Based on the understanding of the group’s ~~organization~~ organisational structure and information system, the auditor may determine that the financial information of certain entities or business units may be considered together for purposes of planning and performing audit procedures. For example, a group may have three legal entities with similar business characteristics, operating in the same geographical location, under the same management, and using a common system of

internal control, including the information system. In these circumstances, the auditor may decide to treat these three legal entities as one component.

Resources

Part 3 requires the engagement partner to determine that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner. The auditor's determination of the resources needed to perform the group audit are a matter of professional ~~judgment~~judgement and may include the understanding of:

- *The group;*
- *The components within the group at which audit work is to be performed, the location of such components and any related jurisdictional factors such as language, culture and regulation; and*
- *Whether to perform work centrally, at components or a combination thereof.*

10.2.2. If, after the acceptance or continuance of the group audit engagement, the engagement partner concludes that sufficient appropriate audit evidence cannot be obtained, the engagement partner shall consider the possible effects on the group audit.

10.3. Materiality

10.3.1. In applying Part 5, when classes of transactions, account balances or disclosures in the group financial statements are disaggregated across components, for purposes of planning and performing audit procedures, the auditor shall determine component performance materiality. To address aggregation risk, such amount shall be lower than group performance materiality.

The component performance materiality amount may be different for each component. Also, the component performance materiality amount for an individual component need not be an arithmetical portion of the group performance materiality and, consequently, the aggregate of component performance materiality amounts may exceed group performance materiality.

The ~~ISA for LCE~~ISA (NZ) for LCE does not require component performance materiality to be determined for each class of transactions, account balance or disclosure for components at which audit procedures are performed. However, if, in the specific circumstances of the group, there is one or more particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the group financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the group financial statements, Part 5 requires a determination of the materiality level or levels to be applied to those particular classes of transactions, account balances or disclosures. In these circumstances, the auditor may need to consider whether a component performance materiality lower than the amount may be appropriate for those particular classes of transactions, account balances or disclosures.

The determination of component performance materiality is not a simple mechanical calculation and involves the exercise of professional ~~judgment~~judgement. Factors the auditor may consider in setting component performance materiality include the following:

- *The extent of disaggregation of the financial information across components (e.g., as the extent of disaggregation across components increases, a lower component performance materiality ordinarily would be appropriate to address aggregation risk). The relative significance of the component to the group may affect the extent of disaggregation (e.g., if a single component represents a large portion of the group, there likely may be less disaggregation across components).*

- *Expectations about the nature, frequency, and magnitude of misstatements in the component financial information, for example the nature and extent of misstatements identified at the component in prior audits.*

To address aggregation risk, paragraph 10.3.1. requires component performance materiality to be lower than group performance materiality. In some circumstances, however, component performance materiality may be set at an amount closer to group performance materiality because there is less aggregation risk, such as when the financial information for one component represents a substantial portion of the group financial statements.

10.4. Understanding the Group and Its Environment, the Applicable Financial Reporting Framework and the Group's System of Internal Control

10.4.1. In applying Part 6, the auditor shall obtain an understanding of:

- (a) The group's ~~organization~~organisation structure and its business model, including:
 - (i) The locations in which the group has its operations or activities;
 - (ii) The nature of the group's operations or activities and the extent to which they are similar across the group; and
 - (iii) The extent to which the group's business model integrates the use of IT.
- (b) The applicable financial reporting framework and the consistency of accounting policies and practices across the group.
- (c) The group's system of internal control, including:
 - (i) The consolidation process used by the group and consolidation adjustments;
 - (ii) The nature and extent of commonality of controls;
 - (iii) How the group ~~centralizes~~centralises activities relevant to financial reporting; and
 - (iv) How group management communicates significant matters that support the preparation of the group financial statements to management of entities or business units.

10.5. ~~Identifying and Assessing the Risks of Material Misstatement~~

10.5.1. In applying Part 6, based on the understanding obtained in paragraph 10.4.1. the auditor shall identify and assess the risks of material misstatement of the group financial statements, including with respect to the consolidation process.

In applying Part 6, the auditor is required to identify and assess the risks of material misstatement of the financial statements due to fraud, and to design and perform further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement due to fraud at the assertion level. Information used to identify the risks of material misstatement of the group financial statements due to fraud may include the following:

- ~~Whether there are particular components that are more susceptible to risks of material misstatement due to fraud.~~
- ~~Whether any fraud risk factors or indicators of management bias exist in the consolidation process.~~
- ~~How those charged with governance of the group monitor group management's processes for identifying and responding to the risks of fraud in the group, and the controls group management has established to mitigate these risks.~~

- ~~_____~~ Responses of those charged with governance of the group, and group management to the auditor's einquiry about whether they have knowledge of any actual, suspected, or alleged fraud affecting a component or the group.

10.6. Responding to the Assessed Risks of Material Misstatement

10.6.1. In applying Part 7, the auditor shall determine the components at which to perform further audit procedures, and the nature, timing and extent of the work to be performed at those components.

Further audit procedures may be designed and performed centrally if the audit evidence to be obtained from performing further audit procedures on one or more significant classes of transactions, account balances or disclosures in the aggregate will respond to the assessed risks of material misstatement, for example, if the accounting records for the revenue transactions of the entire group are maintained centrally.

The auditor may determine that the financial information of components can be considered as a single population for the purpose of performing further audit procedures, for example, when transactions are considered to be homogeneous because they share the same characteristics, the related risks of material misstatement are the same, and controls are designed and operating in a consistent way. In such cases, group performance materiality often will be used for purposes of performing these procedures.

In other circumstances, procedures to respond to the risks of material misstatement of the group financial statements that are related to the financial information of a component may be more effectively performed at the component level. In responding to the assessed risks of material misstatement, the auditor may determine the following scope of work to be appropriate at a component:

- ~~_____~~ Design and perform further audit procedures on the entire financial information of the component;
- ~~_____~~ Design and perform further audit procedures on one or more classes of transactions, account balances or disclosures; or
- ~~_____~~ Perform specific further audit procedures.

Consolidation Process

10.6.2. The auditor shall design and perform further audit procedures to respond to the assessed risks of material misstatement of the group financial statements arising from the consolidation process. This shall include:

- Evaluating whether all entities and business units have been included in the group financial statements as required by the applicable financial reporting framework;
- Evaluating the appropriateness, completeness and accuracy of consolidation adjustments and reclassifications;
- Evaluating whether management's ~~judgment~~ judgements made in the consolidation process give rise to indicators of possible management bias; and
- Responding to assessed risks of material misstatement due to fraud arising from the consolidation process.

The consolidation process may require adjustments and reclassifications to amounts reported in the group financial statements that do not pass through the usual IT applications, and may not be subject to the same controls to which other financial information is subject. The auditor's

evaluation of the appropriateness, completeness and accuracy of the adjustments and reclassifications may include:

- *Evaluating whether significant adjustments appropriately reflect the events and transactions underlying them;*
- *Determining whether those entities or business units whose financial information has been included in the group financial statements were appropriately included;*
- *Determining whether significant adjustments have been correctly calculated, processed and ~~authorized~~authorised by group management and, when applicable, by component management;*
- *Determining whether significant adjustments are properly supported and sufficiently documented; and*
- *Evaluating the reconciliation and elimination of intra-group transactions, unrealized profits, and intra-group account balances.*

10.7. ~~1~~—Specific Communication Requirements

10.7.1. The auditor shall communicate the following matters with those charged with governance:

- (a) An overview of the work to be performed at the components of the group.
- (b) Fraud or suspected fraud involving group management, component management, employees who have significant roles in the group's system of internal control, or others when the fraud resulted in a material misstatement of the group financial statements.

10.8. ~~1~~—Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4, which apply throughout the audit engagement, specific matters to be documented relevant to this Part are described below.

10.8.1. ~~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.

[NZ]11. Audit of Service Performance Information

Content of this Part

Part 11 sets out the considerations that apply when auditing service performance information, concurrently with the financial statements⁵⁷.

Scope of this Part

All parts of the ISA (NZ) for LCE apply when auditing an LCE that reports service performance information and that service performance information is subject to audit⁵⁸. The requirements and guidance in this Part refer to, or expand on, the application of other Parts of the ISA (NZ) for LCE⁵⁹ to the audit of service performance information.

[TBC]Related guidance on the audit of service performance information and examples of modified opinions, can be found in the *Service Performance Information Supplemental Guide*.

11.1. Objectives

~~11.1.1. The objectives of the auditor are:~~

- ~~(a) to obtain reasonable assurance about whether the service performance information is free from material misstatement, whether due to fraud or error, and~~
- ~~(b) to issue an auditor's report that includes their opinion.~~

11.1.1. The objective of the auditor is to express a reasonable assurance opinion on whether the service performance information presents fairly⁶⁰, in all material respects the service performance in accordance with the applicable financial reporting framework.

The auditor may achieve the objectives of this Part by considering the following two steps:

- (a) *Assess whether the following aspects of the service performance information are appropriate and meaningful in accordance with the applicable financial reporting framework:*
- *The elements/aspects of service performance that the entity has selected to report on.*
 - *The performance measures and/or descriptions the entity has used to report on what it has done in relation to those elements/aspects of service performance during the reporting period.*

⁵⁷ When the service performance information is not within the scope of the audit engagement, the auditor's responsibility for the service performance information is limited to following the requirements in Part 9.8.

⁵⁸ Some entities are required by the applicable financial reporting framework to prepare entity information, including Reporting Requirements for Tier 3 Not-for-Profit Entities, Reporting Requirements for Tier 3 Public Sector Entities, Reporting Requirements for Tier 4 Not-for-Profit Entities, Reporting Requirements for Tier 4 Public Sector Entities. For Tier 3 registered charities and incorporated societies, which have a statutory audit requirement (under the Charities Act 2005 or Incorporated Societies Act 2022), all information required to be prepared by the applicable reporting standard is required to be audited, including the entity information. When the entity information is not within scope of the audit engagement, the auditor's responsibility for the entity information is limited to following the requirements in Part 11.18. and Part 9.8.

⁵⁹ In accordance with paragraph NZP.16A, the use of the term "financial statements" in the ISA (NZ) for LCE also refers to "service performance information" and where relevant "entity information" (i.e., where an auditor is applying Part 11).

⁶⁰ When the service performance information is prepared in accordance with a compliance framework, the auditor is not required to evaluate whether the service performance information achieves fair presentation.

- *The measurement basis or evaluation method used to measure or evaluate the performance measure and/or description.*

(b) *Assess whether the reported service performance information fairly reflects the actual service performance and is not materially misstated.*

The auditor may benefit from early engagement with the entity to understand the entity's service performance reporting process, where it intends to report its service performance information and address any challenges that may arise to evaluate whether the service performance information is appropriate and meaningful as required by the ISA (NZ) for LCE.

11.2. Terms of the Audit Engagement

11.2.1. In applying Part 4, the auditor shall agree the terms of the audit engagement with those charged with governance, with respect to the audit of service performance information.

Appendix 2A sets out an illustrative engagement letter including service performance information.

11.3. Planning Activities

11.3.1. In applying Part 5, the auditor shall set the scope, timing and direction of the audit to concurrently cover the service performance information and the financial statements. In doing so, the auditor shall:

- Consider the factors that, in the auditor's professional judgement, are significant in directing the engagement team's efforts in respect of the audit of service performance information;
- Determine the timing of when to evaluate whether the entity's service performance information is appropriate and meaningful; and
- Determine the resources needed to perform the audit engagement in respect of the audit of the service performance information.

Resources

Part 3 requires the engagement partner to determine that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner. The auditor's determination of the resources needed to perform the audit of service performance information are a matter of professional judgement.

~~11.3.2. The auditor shall update and change the scope, timing and direction as necessary during the audit.~~

11.3.2. The auditor shall discuss the following matters with those charged with governance:

- What elements/aspects of service performance and performance measures and/or descriptions the entity intends to report as part of its service performance information;
- What measurement bases or evaluation methods the entity intends to use to measure or evaluate its performance.

11.3.3. Any concerns identified arising from the discussions in 11.3.2. shall then be communicated to those charged with governance as soon as practicable.

Using the Work of Management's Expert

11.3.4. The auditor shall determine whether information to be used as audit evidence has been prepared using the work of a management's expert.

The requirements for when the auditor uses the work of a management's expert are set out in paragraphs 5.2.9. and 7.4.29.

Determining Whether to Use the Work of an Auditor's Expert

11.3.5. If expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence regarding the service performance information, the auditor shall determine whether to use the work of an auditor's expert.

Paragraphs 5.2.10. and 7.4.30. set out the auditor's responsibilities when using the work of an auditor's expert.

11.4. Understanding Relevant Aspects of the Entity and the Service Performance Information

In addition to Part 6.3, the auditor is required to understand the following relevant aspects of the entity for this Part, including the entity and its environment, laws and regulations, the service performance information reported, and the system of internal controls over the preparation of service performance information.

Understanding the Entity and Its Environment

11.4.1. The auditor shall obtain an understanding of:

- (a) ~~Why the entity exists and what it intends to achieve i.e., its purpose or objective and its activities or services the entity performs;~~
- (b) What activities or services the entity performs;
- ~~(c)~~ The entity's primary stakeholders and users of the service performance information; and
- ~~(d)~~ What is considered important to those stakeholders and users identified in ~~(c)~~, and what they may use the service performance information for.

Understanding Laws and Regulations

11.4.2. The auditor shall obtain an understanding of the legal and regulatory framework that specify the form, content, preparation, publication, and audit of service performance information; and how the entity is complying with that framework.

The scope of what service performance information the entity reports may be embodied in law or regulation specific to the entity, industry or sector in which the entity operates and, in particular, with laws and regulations that specify the form and content of service performance information, or which describe the entity's accountability.

The nature of the performance report may be specified in applicable legislation, which may indirectly determine the nature of the performance information to be reported.

The provisions of those laws and regulations may require the entity to present particular service performance information which may be over and above any requirements to comply with the applicable financial reporting framework. As the reporting is required by law and regulation the auditor is not required to assess whether the service performance information is appropriate and meaningful.

Understanding the Service Performance Information Reported

11.4.3. The auditor shall obtain an understanding of:

- (a) The applicable financial reporting framework relevant to the service performance information.
- (b) The process, including the rationale and logic, to determine what elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods and judgements to report.
- (c) The process the entity undertook to identify, ~~and the level of engagement with,~~ the intended users of the service performance information and the level of engagement with the intended users.
- (d) The measurement bases or evaluation methods used by the entity to assess the performance measures and/or descriptions and how these are made available to intended users.
- (e) Changes to the elements/aspects of service performance, performance measures and/or descriptions and the measurement bases or evaluation methods used to report its service performance compared to prior year, planned, forecast or prospective information.
- (f) Where the entity intends to report its service performance information.

In the early stages of reporting service performance information, the entity may not have developed an appropriate process, supported by internal controls, to identify its service performance information, or service performance information may be less accurate or complete. The entity may therefore be unable to include certain aspects of its service performance in its service performance information. The auditor exercises professional judgement to conclude on the impact of such omissions (including those for which the entity has provided reasons or explanations). This is particularly relevant since entities will be at varying stages of maturity in respect of preparing service performance information.

Understanding the Entity's System of Internal Control

11.4.4. The auditor shall obtain an understanding of the control environment relevant to the preparation of the service performance information.

The auditor applies paragraph 6.3.14 to determine whether deficiencies have been identified in the entity's system of internal control.

11.5. Applicable Financial Reporting Framework

11.5.1. The auditor shall evaluate whether the service performance information reported or intended to be reported is in accordance with the applicable financial reporting framework.

Principles and requirements for the reporting of service performance information are specified within the applicable financial reporting framework as follows:

- (a) *For tier 1 and tier 2 public benefit entities: PBE FRS 48 Service Performance Reporting*
- (b) *For tier 3 public benefit entities:*
 - *Reporting Requirements for Tier 3 Not-for-Profit Entities*
 - *Reporting Requirements for Tier 3 Public Sector Entities*
- (c) *For tier 4 public benefit entities:*
 - *Reporting Requirements for Tier 4 Not-for-Profit Entities*
 - *Reporting Requirements for Tier 4 Public Sector Entities.*

Appropriate and Meaningful

11.5.2. The auditor shall evaluate whether the service performance information is appropriate and meaningful including whether:

- (a) It fairly reflects the auditor's understanding of the entity.
- (b) It is likely to meet the needs of the intended users to enable an informed assessment of the entity's service performance.
- (c) It relates to an element/aspect of service performance that significantly contributes to the entity's core purpose, functions or objectives.
- (d) There is likely to be sufficient appropriate evidence to support the performance measure and/or description.
- (e) It is capable of measurement or evaluation in a consistent manner from period to period.
- (f) It is presented in a way that is easy to follow, concise, logical and aggregated where appropriate so that it will enable a user to identify the main points of the entity's service performance in that year.

The discussion at paragraph 11.3.2. may also assist the auditor in their assessment of whether the service performance information the entity intends to report is appropriate and meaningful.

It is important to engage with the entity as early as possible to understand whether the elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods the entity intends to report are appropriate and meaningful.

When evaluating whether the service performance information is appropriate and meaningful, the auditor assesses how well the entity has balanced the qualitative characteristics and pervasive constraints when selecting its elements/aspects of service performance, performance measures and/or descriptions, and measurement bases and evaluation methods.

Laws and Regulations

11.5.3. The auditor shall obtain sufficient appropriate audit evidence that the entity has complied with laws and regulations that have a direct material effect on the reporting of service performance information.

11.6. Materiality

~~11.6.1. The auditor shall:~~

- ~~(a) Using the understanding gained in part 11.4, determine the significant elements/aspects of service performance.~~
- ~~(b) Determine materiality considerations and/or materiality for service performance information~~

11.6.1. The auditor shall:

- (a) Consider materiality for qualitative service performance information; and/or
- (b) Determine materiality for quantitative service performance information.
- (c) For quantitative service performance information, determine performance materiality as applicable in the circumstances.

In considering or determining the materiality for service performance information, the auditor may firstly consider which elements/aspects of service performance are important to intended users, i.e. the significant elements/aspects of service performance. Having identified those, the auditor may then consider what are the material performance measures and/or descriptions that

~~measure performance in those elements/aspects of service performance. A tolerance for misstatement is then applied by the auditor to material service performance measures and/or descriptions.~~

The auditor's understanding of the entity is important in determining what are the significant elements/aspects of the entity's service performance which are important to users of the service performance information. Understanding what elements/aspects of service performance are significant to users may assist the auditor in focusing their audit efforts and applying professional judgement when considering any misstatements identified.

~~Understanding what elements/aspects of service performance are significant to users may assist the auditor in focusing their audit efforts and applying professional judgement when considering any misstatements identified.~~

~~11.6.2. The concept of materiality is applied by the auditor, in both planning and performing the audit, and The auditor shall apply materiality to assess whether:~~

~~(a) The significant elements/aspects of service performance and related material performance measures and/or descriptions are appropriate and meaningful; and~~

~~(b) The service performance information contains individual or collective misstatements, that based on the auditor's judgement, are likely to influence the decisions of the intended users based on the information.~~

The auditor's ~~materiality~~ considerations and/or determination of materiality is a matter of professional judgement. The evaluation required by paragraph 11.5.2. ~~may assist the auditor to consider and/or determine materiality considerations and/or materiality.~~

~~The auditor's determination of materiality is a matter of professional judgement, and is affected by the auditor's perception of the information needs of users of the service performance information.~~

The auditor's professional judgement about misstatements that will be considered material provides a basis ~~determination of materiality considerations and/or materiality provides a basis~~ for:

- ~~Determining the nature, timing and extent of procedures to identify and assess risks of material misstatement;~~
- ~~Identifying and assessing the risks of material misstatement; and~~
- ~~Determining the nature, timing and extent of further audit procedures; and~~

Considering materiality for qualitative service performance information involves the practitioner to actively reflecting upon factors that may lead to potential material misstatements. Examples of factors that may be relevant to the practitioner's consideration of materiality for qualitative service performance information include:

- The importance of the element/aspect of service performance to achieving the entity's service performance objectives.
- How the service performance information is presented.
- The extent of interest shown in particular aspects of service performance by, for example funders, key stakeholders or the public.
- Whether a potential misstatement would be significant based on the practitioner's understanding of known previous communications to the intended users, on matters relevant to the information needs of those users.

~~• The auditor's tolerance for misstatement in relation to material service performance measures and/or descriptions.~~

~~When determining materiality for quantitative service performance information, a percentage is often applied to a chosen benchmark as a starting point. The benchmark for materiality will likely differ from the financial statements. The auditor may need to exercise professional judgement beyond the traditional approach of applying a percentage to a chosen benchmark.~~

~~Materiality may be expressed in terms of the appropriate unit of account for each significant element/aspect of service performance or performance measure and/or description reported. The auditor is unlikely to be able to set an overall materiality because there is unlikely to be a common unit of account.~~

~~The materiality considerations determine the auditor's tolerance for misstatement in relation to material performance measures and/or descriptions. Material misstatements may occur in both qualitative and quantitative service performance information. The auditor may need to exercise professional judgement beyond the traditional approach of applying a % to a chosen benchmark. In some instances, there may be no tolerance for error in some performance measures and/or descriptions.~~

~~Performance materiality does not address misstatements that would be material solely due to qualitative factors. However, designing procedures to increase the likelihood of the identification of misstatements that are material solely because of qualitative factors, to the extent it is possible to do so, may also assist the practitioner in addressing aggregation risk.~~

11.6.2. The auditor shall apply materiality to assess whether:

- ~~(a) The significant elements/aspects of service performance and related material performance measures and/or descriptions are appropriate and meaningful; and~~
- ~~(b) The service performance information contains individual or collective misstatements, that based on the auditor's judgement, are likely to influence the decisions of the intended users based on the information.~~

~~If the auditor's assessment required by paragraph 11.6.2.(a) is that the significant elements/aspects of service performance and related material performance measures and/or descriptions are not appropriate and meaningful, it is a matter of professional judgement as to whether that gives rise to a material misstatement.~~

~~The auditor may firstly consider which elements/aspects of service performance are important to intended users. Having identified those, the auditor may then consider what are the material performance measures and/or descriptions that measure performance in those elements/aspects of service performance. A tolerance for misstatement is then applied by the auditor to material service performance measures and/or descriptions.~~

~~An individual misstatement, impacting a single significant element/aspect of service performance, performance measure and/or description, may be material.~~

~~A number of misstatements, when observed collectively across the service performance information, may also be material if they amount to a misleading portrayal of the entity's service performance information. Even though taken individually, each service performance measure and/or description may not be materially misstated, the auditor needs to consider whether the service performance information as a whole is materially misstated.~~

~~It is unlikely that the auditor will be able to aggregate misstatements numerically. However, this does not remove the need for the auditor to form a conclusion as to whether uncorrected misstatements are material individually or collectively.~~

11.6.23. If the auditor becomes aware of information during the audit that would have caused the auditor to have determined a different materiality initially, the auditor shall revise the materiality considerations and/or materiality for the service performance information.

11.7. Identifying and Assessing the Risks of Material Misstatement

11.7.1. In applying Part 6.2, the auditor shall design and perform procedures to obtain audit evidence that provides an appropriate basis for:

- (a) The identification and assessment of risks of material misstatement, whether due to fraud or error, at service performance information and assertion levels; and
- (b) The design of further audit procedures.

11.7.24. In applying part 6.4. and based on the understanding obtained in part 11.4., the auditor shall identify and assess the risks of material misstatement, whether due to fraud or error, of the service performance information:

- (a) At the service performance information level. In doing so, the auditor shall determine whether they affect risks at the assertion level and consider the nature and extent of the pervasive effect of identified risks on the service performance information; and
- (b) At the assertion level for performance measures, descriptions or disclosures. In doing so, the auditor shall:
 - (i) Determine the relevant assertions and related significant performance measures, descriptions or disclosures; and
 - (ii) Assess inherent risk for identified risks of material misstatement at the assertion level by assessing the likelihood and magnitude of misstatement.

Service Performance Information Level Risks

Risks of material misstatement at the service performance information level refer to risks that relate pervasively to the service performance information as a whole, and potentially affect many assertions. Risks of this nature are not necessarily risks related to specific assertions (e.g., risk of management bias in the selection of service performance information or in the use of language that misleads).

Assertion Level Risks

In identifying and assessing the risks of material misstatement, the auditor uses assertions to consider the different types of potential misstatements that may occur. Appendix 5 sets out assertions that may be used by the auditor in considering different types of misstatements at the assertion level.

An assertion about performance measures, descriptions or disclosures is a relevant assertion when it has an identified risk of material misstatement. The determination of whether an assertion is a relevant assertion is made before consideration of any related controls (i.e., the inherent risk) and is based on the auditor's consideration of misstatements that have a reasonable possibility of both occurring (i.e., likelihood), and being material if they were to occur (i.e., magnitude).

Significant performance measures, descriptions or disclosures are those for which there is one or more relevant assertions. Determining relevant assertions and the significant performance measures, descriptions or disclosures provides a basis for the identification and assessment of risks of material misstatement.

Assessing Inherent Risk

Due to the variation in aggregation, measurement, and presentation of service performance information, the risk assessment is conducted at a meaningful level to reflect the inherent risk of the particular measure.

Significant Risks

In addition to the requirements regarding significant risks in Part 6.4., specific matters relevant to this Part are described below.

11.7.3. The auditor shall determine whether any of the assessed risks of material misstatement of the service performance information are, in the auditor's professional judgement, a significant risk.

Risks of material misstatement that may be assessed as having higher inherent risk, and may therefore be determined to be a significant risk, may arise from matters such as the following:

- *Performance measures that use a measurement basis or evaluation method that may be subject to differing interpretations.*
- *Performance measures that involve complexity in data collection and processing.*
- *Performance measures that use a measurement basis or evaluation method that involves complex calculations.*
- *Changes in the entity's business that involve changes in service performance.*

Paragraph 11.20.1. includes the specific communications requirements in relation to significant risks.

11.8. Audit Procedures Responsive to the Assessed Risks of Material Misstatement

At the Service Performance Information Level

11.8.1. In applying Part 7, tThe auditor shall design and implement overall responses to address the assessed risks of material misstatement at the service performance information level, whether due to fraud or error.

The auditor's overall responses at the service performance information level, for example, making general changes to the nature, timing or extent of audit procedures, or adjustments to resources assigned or using experts, are based on those risks that relate pervasively to the service performance information. These may include, for example, risks arising from industry, regulatory and other external factors. Risks of this nature are not necessarily risks related to specific assertions (e.g., risk of management bias in the selection of service performance information or in the use of language that misleads).

11.8.2. In determining overall responses to address the assessed risks of material misstatement due to fraud at the service performance information level, the auditor shall:

- (a) Evaluate whether the selection of service performance information significant elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods by the entity, particularly those related to subjective measurements, may be indicative of fraudulent reporting of service performance information resulting from management's effort to mislead in the reporting of service performance information; and
- (b) Incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures.

Incorporating an element of unpredictability may be achieved by, for example:

- *Performing substantive procedures on selected elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods not otherwise tested due to their materiality or risk.*
- *Adjusting the timing of audit procedures from that otherwise expected.*
- *Using different sampling methods.*

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

11.8.3. In determining overall responses to address the assessed risks of material misstatement due to fraud at the service performance information level, the auditor shall assign and supervise personnel taking account of the knowledge, skill, and ability of the individuals to be given significant engagement responsibilities and the auditor's assessment of the risks of material misstatement due to fraud for the engagement over the audit of service performance information.

At the Assertion Level

11.8.4. In applying Part 7, the auditor shall design and perform further audit procedures whose nature, timing and extent are based on, and responsive to, assessed risks, whether due to fraud or error, at the assertion level.

Further audit procedures comprise tests of controls and substantive procedures. The auditor may choose to perform tests of controls or they may be required in specific circumstances (see paragraph 11.8.5.(d)). Substantive procedures include tests of details and substantive analytical procedures.

Further audit procedures are responsive to the assessed risk of material misstatement at the assertion level, and provide a clear linkage between the auditor's further procedures and the risk assessment. If the assessed risks of material misstatement are due to fraud risks at the assertion level, the nature, timing and extent of audit procedures may need to be changed to obtain audit evidence that is more relevant and reliable or to obtain additional corroborative information.

The auditor need not design and perform further audit procedures where the assessment of the risk of material misstatement is below the acceptably low level. However, as required by paragraph 11.8.6. irrespective of the assessed risk, the auditor shall perform substantive procedures for all material service performance information.

11.8.5. In designing the further audit procedures, the auditor shall:

- (a) Consider the reasons for the assessment given to the risk of material misstatement at the assertion level for each significant performance measure, description or disclosure, including:
 - (i) The likelihood and magnitude of misstatement due to the characteristics of the significant performance measure, description or disclosure (that is, the inherent risk); and
 - (ii) Whether the risk assessment takes account of controls that address the risk of material misstatements (that is, the control risk), thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively (where the auditor plans to test the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures);
- (b) Obtain more persuasive audit evidence the higher the auditor's assessment of risk;

- (c) In designing and performing tests of controls, obtain more persuasive audit evidence the greater the reliance the auditor places on the operating effectiveness of controls; and
- (d) If the auditor intends to test the operating effectiveness of controls or when substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level, design and perform tests of controls, to obtain sufficient appropriate audit evidence as to the operating effectiveness of such controls.

Internal control systems related to the preparation of service performance may be less developed or less well 'embedded' into the operations than those related to the preparation of financial information. They may be less traditional to those used for financial information and require greater work effort by the auditor to gain an understanding.

In some audits of service performance information, the auditor may not be able to identify many controls, or the extent of documentation prepared by the entity to which they exist or operate may be limited. In such cases, it may be more efficient for the auditor to perform further audit procedures that are primarily substantive procedures.

11.8.6. Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for all material service performance information.

11.9. Sufficient Appropriate Audit Evidence

In addition to the requirements regarding sufficient appropriate audit evidence in Part 2.2. which apply throughout the audit engagement, specific matters relevant to this Part are described below.

11.9.1. The auditor shall obtain sufficient appropriate audit evidence that the:

- (a) **Significant Elements**/aspects of service performance, **and related material** performance measures and/or descriptions, and measurement bases or evaluation methods are appropriate and meaningful; and
- (b) Performance measures and/or descriptions have been prepared in accordance with the entity's measurement bases or evaluation methods; and
- (c) Performance measures and/or descriptions are not materially misstated.

11.9.2. The auditor shall, where possible, draw on the relationships that exist between the service performance information and the financial statements.

The auditor may be able to identify relationships between the service performance information and the financial information as a sense check that the financial information and service performance information are reflecting a consistent report of the performance of the entity.

The auditor may:

- *Agree or reconcile amounts reported in the service performance information to any underlying financial and non-financial records.*
- *Agree cross references between the service performance information and the financial statements.*

11.9.3. The auditor shall obtain sufficient appropriate audit evidence about whether any disclosures of judgements related to service performance information are reasonable in the context of the requirements of the applicable financial reporting framework.

11.10. Evaluation of Misstatements Identified During the Audit of Service Performance Information

11.10.1. In applying Part 8, the auditor shall consider individually or collectively, all misstatements identified, other than those that are clearly trivial, that are uncorrected by the entity, to evaluate whether the service performance information is free from material misstatement.

A misstatement of the service performance information may arise in relation to:

- *The application of the measurement basis or evaluation method;*
- *Inadequate disclosure of judgements made, where applicable; or*
- *Incomplete disclosures that do not include all disclosures required by the applicable financial reporting framework or do not achieve fair presentation of the service performance information*

If the auditor's assessment is that the significant elements/aspects of service performance and related material performance measures and/or descriptions are not appropriate and meaningful, it is a matter of professional judgement as to whether that gives rise to a material misstatement.

Material misstatements may occur in both qualitative and quantitative service performance information. An individual misstatement, impacting a single significant element/aspect of service performance, performance measure and/or description, may be material.

A number of misstatements, when observed collectively across the service performance information, may also be material if they amount to a misleading portrayal of the entity's service performance information. Even though taken individually, each service performance measure and/or description may not be materially misstated, the auditor needs to consider whether the service performance information as a whole is materially misstated.

It is unlikely that the auditor will be able to aggregate misstatements numerically. However, this does not remove the need for the auditor to form a conclusion as to whether uncorrected misstatements are material individually or collectively.

11.11. Written Representations

11.11.1. In applying Part 8, the auditor shall obtain written representations regarding service performance information from those charged with governance, who have appropriate knowledge of the matters concerned and responsibility for the service performance information, that they have fulfilled their responsibility for:

- (a) The selection of elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods that present service performance information that is appropriate and meaningful in accordance with the applicable financial reporting framework.
- (b) The preparation of service performance information in accordance with the entity's measurement bases or evaluation methods, in accordance with the applicable financial reporting framework.
- (c) The overall presentation, structure and content of the service performance information in accordance with the applicable financial reporting framework.

Appendix 7A sets out an illustrative representation letter including service performance information.

11.12. Forming an Opinion on the Service Performance Information

11.12.1. In applying Part 9, the auditor shall form an opinion on whether the service performance information is appropriate and meaningful and prepared, in all material respects, in accordance

with the entity's measurement bases or evaluation methods, in accordance with the applicable financial reporting framework⁶¹.

11.12.2. In order to form that opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the service performance information is free from material misstatement, whether due to fraud or error. That conclusion shall take into account:

- (a) Whether sufficient appropriate audit evidence has been obtained as required by paragraph 11.9.1;
- (b) Whether uncorrected misstatements are material, individually or in aggregate; and
- (c) The evaluations required by paragraphs 11.12.3. to 11.12.6.

11.12.3. The auditor shall evaluate whether the service performance information is prepared, in all material respects, in accordance with the entity's measurement bases or evaluation methods, in accordance with the applicable financial reporting framework.

11.12.4. When the service performance information is prepared in accordance with a fair presentation framework, the auditor shall also evaluate whether the service performance information achieves fair presentation. This evaluation shall include consideration of whether:

- (a) The overall presentation of the service performance information has been undermined by including information that is not relevant or that obscures a proper understanding of the matters disclosed;
- (b) The entity has presented service performance information that is appropriate and meaningful;
- (c) The measurement bases or evaluation methods are available to intended users;
- (d) The overall presentation, structure and content of the service performance information represents the service performance of the entity in a manner that achieves fair presentation; and
- (e) The disclosure of the judgements made in reporting the service performance information, if applicable, is reasonable.

The auditor's evaluation about whether the service performance information achieves fair presentation, is a matter of professional judgement.

11.12.5. The auditor shall consider any matters arising during the audit of the financial statements that may affect the auditor's evaluation of the service performance information.

11.12.6. The auditor shall consider the impacts of any matters arising during the audit of the service performance information that may affect the auditor's evaluation of the financial statements.

11.13. Form of Opinion

11.13.1. The auditor's report on the financial statements and the service performance information shall be included in a single report.

11.13.2. The auditor shall express an unmodified opinion, with respect to the service performance information, when the auditor concludes that the service performance information is prepared, in all material respects, in accordance with the applicable financial reporting framework.

⁶¹ When the service performance information is prepared in accordance with a compliance framework, the auditor is not required to evaluate whether the service performance information achieves fair presentation.

If the financial reporting framework is a fair presentation framework, as is generally the case for general purpose financial reports/ performance reports, the opinion required is on whether the service performance information and financial statements are presented fairly, in all material respects, or give a true and fair view. If the financial reporting framework is a compliance framework, the opinion required is on whether the service performance information and financial statements are prepared, in all material respects, in accordance with the framework.

11.13.3. If service performance information prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor shall discuss the matter with management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, determine whether to modify the opinion.

11.13.4. If the service performance information is prepared in accordance with a compliance framework, the auditor is not required to evaluate whether the service performance information achieves fair presentation. However, if in extremely rare circumstances the auditor concludes, based on the audit evidence obtained, that such service performance information is misleading, the auditor shall discuss the matter with management and, depending on how it is resolved, shall determine whether, and how, to communicate it in the auditor's report.

11.14. Auditor's Report

11.14.1. The auditor shall report in accordance with the specified format and content below unless:

- (a) The auditor's report includes a modified opinion, emphasis of matter paragraph, other matter paragraph, material uncertainty related to going concern, other reporting responsibilities, or a separate section dealing with Other Information, in which case the auditor shall modify the auditor's opinion (according to Part 11.15.) or amend the auditor's report (according to Part 11.18.); or
- (b) The matters in paragraph NZ9.4.1.(a) or NZ9.4.1A. are applicable.

INDEPENDENT AUDITOR'S REPORT

To [Appropriate Addressee]⁶²

Opinion

We have audited⁶³ the [financial report/ performance report] of [ABC Charity (the Entity), which comprise the financial statements on pages x to xx, and the service performance information on pages x to xx [, and entity information on page x]. The complete set of financial statements comprise the statement of financial position as at December 31, 20XX, and the statement of comprehensive revenue and expense, statement of financial performance, statement of changes in net assets/equity, and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information (replace these report names with the appropriate titles)].⁶⁴

In our opinion, the accompanying [financial report/ performance report] presents fairly, in all material respects (or "gives a true and fair view of")⁶⁵:

- [the entity information as at December 31, 20XX;]
- the financial position of the [Entity] as at December 31, 20XX, and its financial performance, and its cash flows for the year then ended; and
- the service performance for the year ended December 31, 20XX in that the service performance information is appropriate and meaningful and prepared in accordance with the [Entity]'s measurement bases or evaluation methods

in accordance with [the applicable financial reporting framework] issued by the New Zealand Accounting Standards Board.⁶⁶

Basis for Opinion

We conducted our audit in accordance with the International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (the ISA (NZ) for LCE). Our responsibilities under the ISA (NZ) for LCE are further described in the *Auditor's Responsibilities for the Audit of the [Financial Report/ Performance Report]* section of our report.⁶⁷ We are independent of the [Entity] in accordance with *Professional and Ethical Standard 1 International Code of Ethics for Assurance Practitioners (including International Independence Standards (New Zealand))* issued by the New Zealand Auditing and Assurance Standards Board, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.⁶⁸

Other than in our capacity as auditor we have no relationship with, or interests in, the [Entity]⁶⁹.

Responsibilities of [Those Charged with Governance] for the [Financial Report/ Performance Report]

[Those Charged with Governance] are responsible on behalf of the [Entity] for:

- The preparation [and fair presentation] of the [financial report/ performance report] in accordance with [applicable financial reporting framework],⁷⁰
- The selection of elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods that present service performance information that is appropriate and meaningful in accordance with the applicable financial reporting framework;
- The preparation and fair presentation of service performance information in accordance with the [Entity's] measurement bases or evaluation methods, in accordance with the applicable financial

reporting framework;

- The overall presentation, structure and content of the service performance information in accordance with the applicable financial reporting framework; and
- Such internal control as [Those Charged with Governance] determine is necessary to enable the preparation of a [financial report/ performance report] that is free from material misstatement, whether due to fraud or error.

In preparing the [financial report/ performance report], [Those Charged with Governance] are responsible for assessing the [Entity's] ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless [Those Charged with Governance] either intends to liquidate the [Entity] or to cease operations, or have no realistic alternative but to do so.

⁶² Matters reflected in the specified format and content of the auditor's report in square brackets (e.g. []) are to be tailored accordingly.

⁶³ When disclaiming an opinion, the statement which indicates that the [financial report/ performance report] have been audited is amended to state that the auditor was engaged to audit the [financial report/ performance report].

⁶⁴ Identify the entity whose [financial report/ performance report] have been audited; identify each financial statement, the statement of service performance, the entity information (if applicable); and its date and period, and refer to the notes and significant accounting policies or use another appropriate description in accordance with the applicable financial reporting framework.

⁶⁵ See also paragraph 11.4.2. When the [financial report/ performance report] is prepared in accordance with a compliance framework, the opinion and description of the auditor's responsibilities refer instead to whether the [financial report/ performance report] is prepared, in all material respects, in accordance with the applicable financial reporting framework.

⁶⁶ Identify the jurisdiction of origin of the financial reporting framework if it is not International Financial Reporting Standards or International Public Sector Accounting Standards as issued by the International Public Sector Accounting Standards Board. For an entity in New Zealand, that is required to apply the New Zealand Accounting Standards Framework, the reference to the applicable financial reporting framework in the auditor's opinion should be to the applicable financial reporting requirements issued by the New Zealand Accounting Standards Board of the External Reporting Board that apply to the tier under which the entity is reporting.

⁶⁷ When the auditor disclaims an opinion on the [financial report/ performance report], this statement is not included in the auditor's report.

⁶⁸ When the auditor expresses a qualified or adverse opinion, the statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion is amended to include the word "qualified" or "adverse", as appropriate. When the auditor disclaims an opinion on the [financial report/ performance report], this statement is not included in the auditor's report.

⁶⁹ If the auditor has any relationship (other than that of auditor) with, or any interests in, the entity, then this statement is amended.

⁷⁰ Where Those Charged with Governance's responsibility is to prepare [financial report/ performance report] that give a true and fair view, this may read: "Those Charged with Governance are responsible for the preparation of a [financial report/ performance report] that gives a true and fair view in accordance with [applicable financial reporting framework], and for such ..."

Auditor's Responsibilities for the Audit of the [Financial Report/ Performance Report]^{71 72}

Our objectives are to obtain reasonable assurance about whether the [financial report/ performance report] as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISA (NZ) for LCE will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this [financial report/ performance report].

As part of an audit in accordance with the ISA (NZ) for LCE, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the [financial report/ performance report], whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the [Entity's] internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by [management and Those Charged with Governance].
- Obtain an understanding of the process applied by the [Entity] to select its elements/aspects of service performance, performance measures and/or descriptions and the measurement bases or evaluation methods.
- Evaluate whether the selection of elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods present an appropriate and meaningful assessment of the [Entity's] service performance in accordance with the applicable financial reporting framework.
- Evaluate whether the service performance information is prepared in accordance with the [Entity's] measurement bases or evaluation methods, in accordance with the applicable financial reporting framework.

⁷¹ The description of the auditor's responsibilities may also be included within an appendix, or refer to a description to the relevant page of the auditors responsibilities on the External Reporting Board's website at <https://www.xrb.govt.nz/standards/assurance-standards/auditors-responsibilities/>. The auditor shall determine that such a description is not inconsistent with this ISA (NZ) for LCE. In such cases, a reference to the location of appendix or description shall be included within the auditor's report, accompanied by "This description forms part of our auditor's report". When the auditor disclaims an opinion, the description of the auditor's responsibilities only includes the matters required by paragraph 9.5.33. – in this context, the reference to financial statements in paragraph 9.5.33. can also be interpreted as service performance information as well.

⁷² When Part 10 applies, further describe the auditor's responsibilities in a group audit engagement by stating that:

- (i) The auditor's responsibilities are to plan and perform the group audit to obtain sufficient appropriate audit evidence regarding the financial information of the entities or business units within the group as a basis for forming an opinion on the group [financial report/ performance report];
- (ii) The auditor is responsible for the direction, supervision and review of the audit work performed for purposes of the group audit; and
- (iii) The auditor remains solely responsible for the auditor's opinion.

- Conclude on the appropriateness of [Those Charged with Governance]’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the [Entity’s] ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the [financial report/ performance report] or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the [Entity] to cease to continue as a going concern.
- [Evaluate the overall presentation, structure and content of the [financial report/ performance report], including the disclosures, and whether the [financial report/ performance report] represent the underlying transactions and events in a manner that achieves fair presentation.]⁷³

We communicate with [management, and where appropriate, those charged with governance] regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

[Signature in the name of the audit firm⁷⁴]

[Auditor Address: name the location in the jurisdiction where the auditor practices]

[Date: No earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor’s opinion on the [financial report/ performance report], including evidence that (i) All the statements and disclosures that comprise the [financial report/ performance report] have been prepared; and (ii) Those with the recognised authority have asserted that they have taken responsibility for the [financial report/ performance report].]

11.14.2. In applying paragraph 9.4.2., when the service performance information is prepared in accordance with a fair presentation framework, the auditor shall refer to “the preparation and fair presentation of the service performance information” or “the preparation of service performance information that give a true and fair view,” as appropriate in the circumstances, in the description of responsibilities for the service performance information in the auditor’s report.

11.14.3. The auditor shall not refer to the work of an auditor’s expert in an auditor’s report containing an unmodified opinion unless required by law or regulation to do so. If such reference is required by law or regulation, the auditor shall indicate in the auditor’s report that the reference does not reduce the auditor’s responsibility for the auditor’s opinion.

11.15. Modifications to the Opinion

Part 9.5. sets out the requirements for which a modified opinion is to be used in different situations, and the form and content of a modified opinion.

The opinion on the financial statements, in many instances, will not be impacted by a modification with respect to the service performance information.

Tables A to C in Part 9.5. may also be relevant when the auditor issues a modified opinion over service performance information. In this context, the use of “financial statements” within these Tables also refers to “service performance information”.

⁷³ Relevant when the [financial report/ performance report] is prepared in accordance with a fair presentation framework.

⁷⁴ [NZ] Law or regulation may require that the auditors’ report include the name of the engagement partner responsible for audits. The auditor may be required by law or regulation, or may decide, to include additional information beyond the engagement partner’s name in the auditor’s report to further identify the engagement partner, for example, the engagement partner’s professional license number that is relevant to where the auditor practices.

11.15.1. The auditor shall modify the opinion in the auditor's report, with respect to the service performance information when:

- (a) The auditor concludes that either individually or collectively the service performance information is elements/aspects of service performance, performance measure and/or descriptions, or measurement bases or evaluation methods are materially misstated in that it is not appropriate and meaningful and as such is not in accordance with the applicable financial reporting framework, or
- (b) The auditor concludes, based on the audit evidence obtained, that the service performance information is not individually or collectively free from material misstatement, or
- (c) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the service performance information, as a whole, is free from material misstatement.

11.15.2. When the auditor modifies the opinion with respect to the service performance information, the auditor shall consider the effect of the modification on the opinion on the financial statements.

11.15.3. When the auditor modifies the audit opinion with respect to the service performance information only, the audit opinion shall clearly indicate that the opinion on the financial statements is not modified. The auditor shall use the headings "Qualified Opinion on the Service Performance Information", "Adverse Opinion on the Service Performance Information" or "Disclaimer of Opinion on the Service Performance Information" as appropriate. The opinion with respect to the financial statements shall use the heading "Opinion on the Financial Statements".

11.15.4. If the auditor modifies the opinion on the financial statements, the auditor shall consider the effect of the modification on the opinion on the service performance information.

11.16. Other Paragraphs in the Auditor's Report

Part 9.6. sets out when Emphasis of Matter paragraphs and Other Matter paragraphs in the auditor's report are used.

In the context of an audit of service performance information, an Emphasis of Matter paragraph or an Other Matter paragraph may describe for example:

- *The underlying facts and information about the entity's process to select what service performance to report on (e.g., the maturity of the entity's process compared to others in the industry).*
- *The source and method used to measure or evaluate the service performance information and whether they are externally established (e.g., established in legislation or externally established performance frameworks).*
- *Any significant interpretations made in selecting the entity's service performance information or applying the method(s) to measure or evaluate.*
- *Whether there have been any changes in the service performance information disclosed or measurement bases or evaluation methods used.*
- *Any other matters the auditor considers necessary to assist intended users in making decisions based on the service performance information.*
- *Information the auditor considers would enhance transparency and assist the user to understand the level of maturity that the entity has achieved in its reporting.*

Emphasis of Matter Paragraphs

11.16.1. If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the service performance information that, in the auditor's professional judgement, is of such importance that it is fundamental to the users' understanding of the service performance information, and the auditor would not be required to modify the opinion as a result of that matter, the auditor shall include an Emphasis of Matter paragraph in the auditor's report indicating that the auditor's report is not modified in respect of the matter emphasised.

Other Matter Paragraphs

11.16.2. If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the service performance information that, in the auditor's professional judgement, is relevant to the users' understanding of the audit, the auditor's responsibilities or the auditor's report the auditor shall include an Other Matter paragraph in the auditor's report provided this is not prohibited by law or regulation.

11.17. Comparative and Prospective Service Performance Information*Comparative Service Performance Information*

11.17.1. In applying part 9.7, the auditor shall determine whether:

- (a) Prior period comparative service performance information agrees with disclosures presented in the prior period or when appropriate, have been restated; and
- (b) The elements/aspects of service performance, performance measure and/or descriptions, or measurement bases or evaluation methods is consistent with the current period or, if there have been changes, whether those changes have been properly accounted for and adequately presented and disclosed.

Prospective Service Performance Information

11.17.2. Where the entity presents a comparison of published prospective service performance information with the service performance information, the auditor shall:

- (a) Assess whether the prospective service performance information agrees with the information presented in the published prospective service performance information; or
- (b) Assess that any changes have been properly accounted for and adequately presented and disclosed.

11.18. Other Information

"Other information" is financial or non-financial information (other than the financial statements, service performance information and the auditor's report thereon) included in an entity's annual report.

In the context of service performance information, the distinction between the audited service performance information and the "other information" is not as pronounced as it is for financial information. As a consequence, quite subtle changes in the way that information is presented in the "other information" (such as wording used to describe performance) may provide a misleading impression of the entity's actual performance when compared to the audited service performance information.

11.18.1. In applying Part 9.8, the auditor shall read the other information, and:

- (a) Consider whether there is a material inconsistency between the other information and the service performance information; and

- (b) Consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained in the audit.

11.19. Specific Focus Areas

Using the Services of a Service Organisation

11.19.1. In applying parts [6.3 and 7.4](#), if the entity is using the services of a service organisation in the context of service performance information, the auditor shall:

- (a) Determine whether sufficient appropriate audit evidence concerning the relevant service performance information assertions is available at the entity; and, if not,
- (b) Perform further audit procedures to obtain sufficient appropriate audit evidence.

To obtain sufficient appropriate audit evidence, the following procedures may be considered by the auditor:

- *Inspect records and documents held by the user entity;*
- *Inspect records and documents held by the service organisation;*
- *Obtain confirmations of service performance information from the service organisation in instances where the user entity maintains its own independent records of service performance information.*

Audit of Group Service Performance Information

11.19.2. If applying Part 10, the auditor shall obtain sufficient appropriate audit evidence regarding:

- (a) the service performance information of the components; and
- (b) the aggregation or consolidation process as it relates to the service performance information.

11.20. Specific Communication Requirements

11.20.1. The auditor shall communicate, unless prohibited by law and regulation, the following matters with those charged with governance:

- (a) Any significant risks identified with the service performance information.
- (b) The auditor's views about significant judgements made in reporting the entity's service performance information, including any significant deficiencies or areas for improvement.
- (c) Significant difficulties, if any, encountered during the audit of service performance information.
- (d) Unless all of those charged with governance are involved in managing the entity, significant matters arising during the audit that were discussed, or subject to correspondence with management.
- (e) Matters involving non-compliance with laws and regulations with respect to service performance [information](#) reporting obligations.
- (f) Deficiencies in internal control with respect to the service performance information that, in the auditor's professional judgement, are of sufficient importance to merit attention.
- (g) Uncorrected misstatements and the effect that they, individually or in aggregate, may have on the opinion on the service performance information in the auditor's report and request that they are corrected.

- (h) Any modifications including the circumstances and the wording the auditor expects to make to the opinion relating to service performance information in the auditor's report.

11.21. Specific Documentation Requirements

In addition to the general documentation requirements in Part 2.4. which apply throughout the audit engagement, and other documentation requirements in this standard which may apply to the audit of service performance information, specific matters to be documented relevant to this Part are described below.

~~11.21.1. In addition to the requirements of paragraph NZ4.7.4., the audit engagement letter or other suitable form of written agreement shall include the objective and scope of the audit, and the respective responsibilities of the auditor and those charged with governance, with respect to the service performance information.~~

~~11.21.2. In applying paragraph 11.6.1., the auditor shall document materiality considerations and/or materiality for service performance information.~~

~~11.21.3. The auditor shall include in the audit documentation as far as possible, evidence of relevant relationships between the service performance information and the financial statements.~~

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

- (a) The audit engagement letter or other suitable form of written agreement shall include the requirements of paragraph NZ4.7.4, as well as the following with respect to service performance information:
 - (i) The objective and scope of the audit, and
 - (ii) The respective responsibilities of the auditor and those charged with governance,
 - (iii) Identification of the applicable financial reporting framework,
 - (iv) Reference to the expected form and content of any reports to be issued by the auditor;
- (b) The identified significant elements/aspects of service performance;
- (c) The factors relevant to the practitioner's consideration of materiality for qualitative service performance information;
- (d) The basis for the determination of materiality for quantitative service performance information;
- (e) The basis for the determination of performance materiality
- (f) The overall responses to the assessed risks of material misstatement at the service performance information level;
- (g) The linkage between the procedures performed and the assessed risks at the assertion level;
- (h) The results of the audit procedures, including the conclusions where these are not otherwise clear;
- (i) All misstatements accumulated during the audit and whether they have been corrected; and
- (j) As far as possible, evidence of relevant relationships between the service performance information and the financial statements.

APPENDIX 1

Glossary of Terms

This glossary lists the terms that are defined for the purpose of the ~~ISA for LCE~~ ISA (NZ) for LCE. The definitions assist in the consistent application and interpretation of this standard, and are not intended to override definitions that may be established for other purposes, whether in law or regulation or otherwise. Unless otherwise indicated, the definitions carry the same meanings throughout this standard. In addition, this glossary includes descriptions of other terms found in the ~~ISA for LCE~~ ISA (NZ) for LCE to assist in common and consistent interpretation and translation (such other terms are identified by an asterisk “*”).

Accounting estimate—A monetary amount for which the measurement, in accordance with the requirements of the applicable financial reporting framework, is subject to estimation uncertainty.

Accounting records—The records of initial accounting entries and supporting records, such as ~~checks~~ **and** records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in formal journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures.

Aggregation risk—The probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statement as a whole.

Analytical procedures—Evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

Annual report—A document, or combination of documents, prepared typically on an annual basis by management or those charged with governance in accordance with law, regulation or custom, the purpose of which is to provide owners (or similar stakeholders) with information on the entity’s operations and the entity’s financial results and financial position as set out in the financial statements. An annual report contains or accompanies the financial statements and the auditor’s report thereon and usually includes information about the entity’s developments, its future outlook and risks and uncertainties, a statement by the entity’s governing body, and reports covering governance matters.

Anomaly—A misstatement or deviation that is demonstrably not representative of misstatements or deviations in a population.

Applicable financial reporting framework—The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

The term “fair presentation framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

- (a) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
- (b) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.

Appropriateness (of audit evidence)—The measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based.

Arm’s length transaction—A transaction conducted on such terms and conditions as between a willing buyer and a willing seller who are unrelated and are acting independently of each other and pursuing their own best interests.

* **Assess**—Analyze identified risks of material misstatement to conclude on their significance. “Assess,” by convention, is used only in relation to risk. (also see *Evaluate*)

Assertions—Representations, explicit or otherwise, with respect to the recognition, measurement, presentation and disclosure of information in the financial statements which are inherent in management representing that the financial statements are prepared in accordance with the applicable financial reporting framework. Assertions are used by the auditor to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement.

Assurance—(see *Reasonable assurance*)

[NZ] Assurance practitioner—A person or an organisation, whether in public practice, industry, commerce or the public sector, appointed or engaged to undertake assurance engagements or related services.

Audit documentation—The record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached (terms such as “working papers” or “workpapers” are also sometimes used).

Audit evidence—Information used by the auditor in arriving at the conclusions on which the auditor’s opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information. (See *Sufficiency of audit evidence* and *Appropriateness of audit evidence*.)

Audit file—One or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement.

Audit firm—(see *Firm*)

Audit opinion—(see *Modified opinion and Unmodified opinion*)

Audit risk—The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

Audit sampling (sampling)—The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

Auditor—“Auditor” is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where the ~~ISA for LCE~~ **ISA (NZ) for LCE** expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term “engagement partner” rather than “auditor” is used. “Engagement partner” and “firm” are to be read as referring to their public sector equivalents where relevant.

Auditor’s expert—An individual or ~~organization~~ **organisation** possessing expertise in a field other than

accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence. An auditor's expert may be either an auditor's internal expert (who is a partner⁷⁵ or staff, including temporary staff, of the auditor's firm or a network firm), or an auditor's external expert.

Auditor's point estimate or auditor's range—An amount, or range of amounts, respectively, developed by the auditor in evaluating management's point estimate.

Auditor's range—(see Auditor's point estimate)

Business risk—A risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity's ability to achieve its objectives and execute its strategies, or from the setting of inappropriate objectives and strategies.

Comparative financial statements—Comparative information where amounts and other disclosures for the prior period are included for comparison with the financial statements of the current period but, if audited, are referred to in the auditor's opinion. The level of information included in those comparative financial statements is comparable with that of the financial statements of the current period.

Comparative information—The amounts and disclosures included in the financial statements in respect of one or more prior periods in accordance with the applicable financial reporting framework.

Compliance framework—(see *Applicable financial reporting framework* and *General purpose framework*)

Component—An entity, business unit, function or business activity, or some combination thereof, determined by the auditor for purposes of planning and performing audit procedures in a group audit.

Component auditor—An auditor who performs audit work related to a component for purposes of the group audit. A component auditor is a part of the engagement team for a group audit.

Component management—Management responsible for a component.

Component performance materiality—An amount set by the auditor to reduce aggregation risk to an appropriately low level for purposes of planning and performing audit procedures in relation to a component.

* **Control activities**—Those policies and procedures that help ensure that management directives are carried out. Control activities are a component of internal control.

* **Control environment**—Includes the governance and management functions and the attitudes, awareness and actions of those charged with governance and management concerning the entity's internal control and its importance in the entity. The control environment is a component of internal control.

Control risk—(see *Risk of material misstatement*)

* **Controls at the service ~~organization~~organisation**—Controls over the achievement of a control objective that is covered by the service auditor's assurance report.

* **Corporate governance**—(see *Governance*)

Corresponding figures—Comparative information where amounts and other disclosures for the prior period are included as an integral part of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as "current period figures"). The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.

⁷⁵ "Partner" and "firm" should be read as referring to their public sector equivalents where relevant.

Controls—Policies or procedures that an entity establishes to achieve the control objectives of management or those charged with governance. In this context:

- (a) Policies are statements of what should, or should not, be done within the entity to effect control. Such statements may be documented, explicitly stated in communications, or implied through actions and decisions.
- (b) Procedures are actions to implement policies.

Date of approval of the financial statements—The date on which all the statements that comprise the financial statements, including the related notes, have been prepared and those with the ~~recognized~~recognised authority have asserted that they have taken responsibility for those financial statements.

Date of the auditor's report—The date the auditor dates the report on the financial statements.

Date of the financial statements—The date of the end of the latest period covered by the financial statements.

Date the financial statements are issued—The date that the auditor's report and audited financial statements are made available to third parties.

Deficiency in internal control—This exists when:

- (a) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis; or
- (b) A control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing.

Detection risk—The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

Emphasis of Matter paragraph—A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's ~~judgment~~judgement, is of such importance that it is fundamental to users' understanding of the financial statements.

* **Engagement letter**—Written terms of an engagement in the form of a letter.

Engagement partner⁷⁶—The partner or other individual, appointed by the firm, who is responsible for the audit engagement and its performance, and for the auditor's report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

[NZ] Public Sector Considerations

Engagement partner includes an employee of the Auditor-General, whom the Auditor-General has appointed under the Public Audit Act 2001 to act as an auditor and who: (i) Is responsible for the engagement and its performance, and for the report that is issued on behalf of the Auditor-General; and (ii) Where required, has the appropriate authority from a professional, legal or regulatory body.

Engagement quality review—An objective evaluation of the significant ~~judgment~~judgements made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report.

⁷⁶ "Engagement partner," "partner," and "firm" is to be read as referring to their public sector equivalents where relevant.

Engagement quality reviewer—A partner, other individual in the firm, or an external individual, appointed by the firm to perform the engagement quality review.

Engagement team—All partners and staff performing the audit engagement, and any other individuals who perform audit procedures on the engagement, excluding an auditor's external expert and internal auditors who provide direct assistance on an engagement.

*** Enquiry**—Enquiry consists of seeking information of knowledgeable persons, both financial and non-financial, within the entity or outside the entity.

*** Error**—An unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

Estimation uncertainty—Susceptibility to an inherent lack of precision in measurement.

*** Evaluate**—Identify and analyzeanalyse the relevant issues, including performing further procedures as necessary, to come to a specific conclusion on a matter. "Evaluation," by convention, is used only in relation to a range of matters, including evidence, the results of procedures and the effectiveness of management's response to a risk. (also see Assess)

Exception—A response that indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party.

Experienced auditor—An individual (whether internal or external to the firm) who has practical audit experience, and a reasonable understanding of:

- (a) Audit processes;
- (b) The ~~ISA for LCE~~ ISA (NZ) for LCE and applicable legal and regulatory requirements;
- (c) The business environment in which the entity operates; and
- (d) Auditing and financial reporting issues relevant to the entity's industry.

Expert—(see *Auditor's expert* and *Management's expert*)

Expertise—Skills, knowledge and experience in a particular field.

External confirmation—Audit evidence obtained as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.

External information source—An external individual or organizationorganisation that provides information that has been used by the entity in preparing the financial statements, or that has been obtained by the auditor as audit evidence, when such information is suitable for use by a broad range of users. When information has been provided by an individual or organizationorganisation acting in the capacity of a management's expert, service organizationorganisation, or auditor's expert the individual or organizationorganisation is not considered an external information source with respect to that particular information.

Fair presentation framework—(see *Applicable financial reporting framework* and *General purpose framework*)

Financial statements—A structured representation of historical financial information, including disclosures, intended to communicate an entity's economic resources or obligations at a point in time, or the changes therein for a period of time, in accordance with a financial reporting framework. The term "financial statements" ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement. Disclosures comprise explanatory or descriptive information, set out as required, expressly permitted or otherwise allowed by the applicable financial reporting framework, on the face of a financial statement, or in the notes, or incorporated therein by cross-reference.

[NZ] Firm—A sole practitioner, partnership or corporation or other entity of ~~professional assurance practitioners~~~~accountants~~, or public sector equivalent.

Public Sector Considerations

Firm includes the Auditor-General as defined in section 10(1) of the Public Audit Act 2001.

Fraud—An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

Fraud risk factors—Events or conditions that indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud.

* **Fraudulent financial reporting**—Involves intentional misstatements, including omissions of amounts or disclosures in financial statements, to deceive financial statement users.

* **Further procedures**—Procedures performed in response to assessed risks of *material* misstatement, including tests of controls (if any), tests of details and analytical procedures.

General purpose financial statements—Financial statements prepared in accordance with a general purpose framework.

General information technology (IT) controls—Controls over the entity's IT processes that support the continued proper operation of the IT environment, including the continued effective functioning of information processing controls and the integrity of information (i.e., the completeness, accuracy and validity of information) in the entity's information system. Also see the definition of *IT environment*.

General purpose framework—A financial reporting framework designed to meet the common financial information needs of a wide range of users. The financial reporting framework may be a fair presentation framework or a compliance framework.

The term “fair presentation framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

- (a) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
- (b) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.

Group financial statements—Financial statements that include the financial information of more than one entity or business unit through a consolidation process. For purposes of the ~~ISA for LCE~~ISA (NZ) for LCE, a consolidation process includes:

- (a) Consolidation, proportionate consolidation, or an equity method of accounting;
- (b) The presentation in combined financial statements of the financial information of entities or business units that have no parent but are under common control or common management; or

The aggregation of the financial information of entities or business units such as branches or divisions.

~~* **Inquiry**—Inquiry consists of seeking information of knowledgeable persons, both financial and non-financial, within the entity or outside the entity.~~

Internal audit function—A function of an entity that performs assurance and consulting activities designed to evaluate and improve the effectiveness of the entity’s governance, risk management and internal control processes.

* **Internal auditors**—Those individuals who carry out the activities of the internal audit function. Internal auditors may belong to an internal audit department or similar function.

* **Internal control**—The process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity’s objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. The term “controls” refers to any aspects of one or more of the components of internal control.

International Financial Reporting Standards—The International Financial Reporting Standards issued by the International Accounting Standards Board.

Non-compliance (in the context of laws and regulations)—Acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees. Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

[NZ] Misstatement (in the context of Part 11)—Misstatements can be intentional or unintentional, qualitative or quantitative, and include omissions. Misstatements can arise from error or fraud when:

- (i) An element/aspect of service performance or performance measure and/or description, or a measurement basis or evaluation method is not appropriate and meaningful; or
- (ii) An element/aspect of service performance or performance measure and/or description that would be appropriate and meaningful is omitted; or
- (iii) Incorrectly measuring or evaluating the entity’s service performance.

Non-response—A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered.

* **Observation**—Consists of looking at a process or procedure being performed by others, for example, the auditor’s observation of inventory counting by the entity’s personnel, or of the performance of control activities.

Opening balances—Those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

Other information—Financial or non-financial information (other than financial statements and the auditor’s report thereon) included in an entity’s annual report.

Other Matter paragraph—A paragraph included in the auditor’s report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor’s ~~judgment~~judgement, is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report.

Outcome of an accounting estimate—The actual monetary amount which results from the resolution of the underlying transaction(s), event(s) or condition(s) addressed by the accounting estimate.

[NZ] Partner—Any individual with authority to bind the firm with respect to the performance of an professional services engagement governed by the Standards of the XRB (including audits or reviews of financial statements, or other assurance or related services engagements⁷⁷).

Public Sector Considerations

Partner includes an employee of the Auditor-General with authority to bind the Auditor-General with respect to the performance of an engagement governed by the Standards of the XRB (including audits or reviews of financial statements, or other assurance or related services engagements).

Performance materiality—The amount or amounts set by the auditor at less than materiality for the financial statements as a whole 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, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, account balances or disclosures.

Personnel—Partners and staff of the firm.

Pervasive—A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence. Pervasive effects on the financial statements are those that, in the auditor's ~~judgment~~**judgement**:

- (a) Are not confined to specific elements, accounts or items of the financial statements;
- (b) If so confined, represent or could represent a substantial proportion of the financial statements;
or
- (c) In relation to disclosures, are fundamental to users' understanding of the financial statements.

Population—The entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions.

Positive confirmation request—A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

~~* **Practitioner**—A professional accountant in public practice.~~

Preconditions for an audit—The use by management of an acceptable financial reporting framework in the preparation of the financial statements and the agreement of management and, where appropriate, those charged with governance to the premise on which an audit is conducted.

Predecessor auditor—The auditor from a different audit firm, who audited the financial statements of an entity in the prior period and who has been replaced by the current auditor.

Premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted—That management and, where appropriate, those charged with governance have acknowledged and understand that they have the following responsibilities that are fundamental to the conduct of an audit in accordance with the ~~ISA for LCE~~**ISA (NZ) for LCE**. That is, responsibility:

- (a) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;

⁷⁷ [NZ] As defined by XRB Au 1 *Application of Auditing and Assurance Standards (Legislative Update)*.

- (b) For such internal control as management and, where appropriate, those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
- (c) To provide the auditor with:
 - (i) Access to all information of which management and, where appropriate, those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - (ii) Additional information that the auditor may request from management and, where appropriate, those charged with governance for the purpose of the audit; and
 - (iii) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

In the case of a fair presentation framework, (a) above may be restated as “for the preparation and *fair* presentation of the financial statements in accordance with the financial reporting framework,” or “for the preparation of financial statements *that give a true and fair view* in accordance with the financial reporting framework.”

The “premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted” may also be referred to as the “premise.”

~~* **Professional accountant**⁷⁸—An individual who is a member of an IFAC member body.~~

~~* **Professional accountant in public practice**⁷⁹—A professional accountant, irrespective of functional classification (for example, audit, tax or consulting) in a firm that provides professional services. This term is also used to refer to a firm of professional accountants in public practice.~~

Professional judgment~~judgement~~—The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

Professional skepticism~~scepticism~~—An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of evidence.

[NZ] Professional standards—~~In the context of this standard, the~~ International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE) and relevant ethical requirements ~~issued by the External Reporting Board or the New Zealand Auditing and Assurance Standards Board.~~

* **Public sector**—National governments, regional (for example, state, provincial, territorial) governments, local (for example, city, town) governments and related governmental entities (for example, agencies, boards, commissions and enterprises).

Reasonable assurance (in the context of audit engagements)—A high, but not absolute, level of assurance.

* **Recalculation**—Consists of checking the mathematical accuracy of documents or records.

Related party—A party that is either:

- (a) A related party as defined in the applicable financial reporting framework; or

- (b) Where the applicable financial reporting framework establishes minimal or no related party requirements:
- (i) A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;
 - (ii) Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
 - (iii) Another entity that is under common control with the reporting entity through having:
 - a. Common controlling ownership;
 - b. Owners who are close family members; or
 - c. Common key management.

However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another.

Relevant assertions—An assertion about a class of transactions, account balance or disclosure is relevant when it has an identified risk of material misstatement. The determination of whether an assertion is a relevant assertion is made before consideration of any related controls (i.e., the inherent risk).

[NZ] Relevant ethical requirements—Principles of professional ethics and ethical requirements that are applicable to professional accountants when undertaking the audit engagement. Relevant ethical requirements in New Zealand ordinarily comprise the provisions of the Professional and Ethical Standard 1, International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand) related to audits of financial statements. ~~International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) related to audits of financial statements, together with national requirements that are more restrictive.~~

* **Reperformance**—The auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal controls.

Risks arising from the use of IT—Susceptibility of information processing controls to ineffective design or operation, or risks to the integrity of information (i.e., the completeness, accuracy and validity of transactions and other information) in the entity's information system, due to ineffective design or operation of controls in the entity's IT processes (see IT environment).

Risk of material misstatement—The risk that the financial statements are materially misstated prior to audit. This consists of two components, described as follows at the assertion level:

- (a) **Inherent risk**—The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
- (b) **Control risk**—The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control.

[NZ] Risk of material misstatement (in the context of Part 11)—The risk that the service performance information is materially misstated prior to the audit. This consists of two components, described as follows at the assertion level:

- (i) Inherent risk – The susceptibility of an assertion about a performance measure and/or description, measurement basis or evaluation method or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
- (ii) Control risk – The risk that a misstatement that could occur in an assertion about a performance measure and/or description, measurement basis or evaluation method or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity’s system of internal controls.

Sampling—(see *Audit sampling*)

Sampling risk—The risk that the auditor’s conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions:

- (a) In the case of a test of controls, that controls are more effective than they actually are, or in the case of a test of details, that a material misstatement does not exist when in fact it does. The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion.
- (b) In the case of a test of controls, that controls are less effective than they actually are, or in the case of a test of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect.

Sampling unit—The individual items constituting a population.

Service auditor—An auditor who, at the request of the service ~~organization~~organisation, provides an assurance report on the controls of a service ~~organization~~organisation.

Service ~~organization~~organisation—A third-party ~~organization~~organisation (or segment of a third-party ~~organization~~organisation) that provides services to user entities that are relevant to a user entity’s process to prepare its financial statements .

* **Significance**—The relative importance of a matter, taken in context. The significance of a matter is judged by the practitioner in the context in which it is being considered. This might include, for example, the reasonable prospect of its changing or influencing the decisions of intended users of the practitioner’s report; or, as another example, where the context is a ~~judgment~~judgement about whether to report a matter to those charged with governance, whether the matter would be regarded as important by them in relation to their duties. Significance can be considered in the context of quantitative and qualitative factors, such as relative magnitude, the nature and effect on the subject matter and the expressed interests of intended users or recipients.

Significant class of transactions, account balance or disclosure—A class of transactions, account balance or disclosure for which there is one or more relevant assertions.

Significant deficiency in internal control—A deficiency or combination of deficiencies in internal control that, in the auditor’s professional ~~judgment~~judgement, is of sufficient importance to merit the attention of those charged with governance.

Significant risk—An identified risk of material misstatement:

- (a) For which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the significance of the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur; or

- (b) That is to be treated as a significant risk in accordance with the requirements of the ~~ISA for LCE~~ISA (NZ) for LCE.

Special purpose financial statements—Financial statements prepared in accordance with a special purpose framework.

Special purpose framework—A financial reporting framework designed to meet the financial information needs of specific users. The financial reporting framework may be a fair presentation framework or a compliance framework.

Statistical sampling—An approach to sampling that has the following characteristics:

- (a) Random selection of the sample items; and
 (b) The use of probability theory to evaluate sample results, including measurement of sampling risk.

A sampling approach that does not have characteristics (a) and (b) is considered non-statistical sampling.

Stratification—The process of dividing a population into sub-populations, each of which is a group of sampling units which have similar characteristics (often monetary value).

Subsequent events—Events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.

Substantive procedure—An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise:

- (a) Tests of details (of classes of transactions, account balances, and disclosures); and
 (b) Substantive analytical procedures.

Sufficiency (of audit evidence)—The measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence.

System of internal control—The system designed, implemented and maintained by those charged with governance, management and other personnel, to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

* **Test**—The application of procedures to some or all items in a population.

Tests of controls—An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level.

Those charged with governance—The person(s) or ~~organization~~organisation(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Tolerable misstatement—A monetary amount set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the monetary amount set by the auditor is not exceeded by the actual misstatement in the population.

Tolerable rate of deviation—A rate of deviation from prescribed internal control procedures set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the rate of deviation set by the auditor is not exceeded by the actual rate of deviation in the population.

Uncorrected misstatements—Misstatements that the auditor has accumulated during the audit and that have not been corrected.

Unmodified opinion—The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

User entity—An entity that uses a service ~~organization~~organisation and whose financial statements are being audited.

Walk-through test (or Walk-through)—Involves tracing a few transactions through the financial reporting system.

Written representation—A written statement by management provided to the auditor to confirm certain matters or to support other audit evidence. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records.

Illustrative Engagement Letter

The following is an illustrative engagement letter for an audit of general purpose financial statements prepared in accordance with [applicable financial reporting framework]. This letter is not authoritative but is intended only to be a guide that may be used in conjunction with the considerations outlined in the ~~ISA for LCE~~ ISA (NZ) for LCE. It will need to be varied according to individual requirements and circumstances. It is drafted to refer to the audit of financial statements for a single reporting period and would require adaptation if intended or expected to apply to recurring audits (see paragraph 4.4.2). It may be appropriate to seek legal advice that any proposed letter is suitable.

To the appropriate representative of ~~management or~~ those charged with governance of ABC Company:⁸⁰

[The objective and scope of the audit]

You⁸¹ have requested that we audit the financial statements of [ABC Company (the "entity")], which comprise the statement of financial position as at December 31, 20X+X, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies. We are pleased to confirm our acceptance and our understanding of this audit engagement by means of this letter.

The objectives of our audit are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (~~ISA for LCE~~ ISA (NZ) for LCE) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

[The responsibilities of the auditor]

We will conduct our audit in accordance with the ~~ISA for LCE~~ ISA (NZ) for LCE. The ~~ISA for LCE~~ ISA (NZ) for LCE requires that we comply with ethical requirements. As part of an audit in accordance with the ~~ISA for LCE~~ ISA (NZ) for LCE, we exercise professional ~~judgment~~ judgement and maintain professional ~~skepticism~~ scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Understand internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the

⁸⁰ The addressees and references in the letter would be those that are appropriate in the circumstances of the engagement, including the relevant jurisdiction.

⁸¹ Throughout this letter, references to "you," "we," "us," "management," "those charged with governance" and "auditor" would be used or amended as appropriate in the circumstances.

effectiveness of the entity's internal control. However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the financial statements that we have identified during the audit.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by [management and those charged with governance].
- Conclude on the appropriateness of [management's/those charged with governance's] use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's—entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company—entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with the ISA for LCE/ISA (NZ) for LCE.

[The responsibilities of management—those charged with governance and identification of the applicable financial reporting framework]⁸²

Our audit will be conducted on the basis that ~~[management, and where appropriate,~~ those charged with governance]⁸³ acknowledge and understand that they have responsibility on behalf of the entity:

- ~~(a)~~—For the preparation [and fair presentation] of the financial statements in accordance with [applicable financial reporting framework];⁸⁴
- ~~(b)~~—For such internal control as ~~[management/they]~~ determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
- ~~(c)~~—To provide us with:
 - (i) Access to all information of which [management and those charged with governance] is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - (ii) Additional information that we may request from [management and those charged with governance] for the purpose of the audit; and
 - (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

⁸² For purposes of this illustrative engagement letter, it is assumed that the auditor has not determined that the law or regulation prescribes those responsibilities in appropriate terms; the descriptions in paragraph 4.2.1(b) of this standard are therefore used)

⁸³ Use terminology as appropriate in the circumstances.

⁸⁴ Or, if appropriate, "For the preparation of financial statements that give a true and fair view in accordance with [applicable financial reporting framework]"

As part of our audit process, we will request from [~~management, and where appropriate,~~ those charged with governance], written confirmation concerning representations made to us in connection with the audit.

We look forward to full cooperation from your staff during our audit.

[Other relevant information]

[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]

[Reporting]

[Insert appropriate reference to the expected form and content of the auditor's report including, if applicable, the reporting on other information.]

The form and content of our report may need to be amended in the light of our audit findings.

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of the financial statements including our respective responsibilities.

XYZ & Co.

Acknowledged and agreed on behalf of ABC Company by

(signed)

.....

Name and Title

Date

[NZ] APPENDIX 2A**Illustrative Engagement Letter including Service Performance Information**

The following is an illustrative engagement letter for an audit of a [financial report/ performance report], which comprise financial statements and service performance information, prepared in accordance with [applicable financial reporting framework]. This letter is not authoritative but is intended only to be a guide that may be used in conjunction with the considerations outlined in the ISA (NZ) for LCE. It will need to be varied according to individual requirements and circumstances. It is drafted to refer to the audit of a [financial report/ performance report] for a single reporting period and would require adaptation if intended or expected to apply to recurring audits (see paragraph 4.4.2). It may be appropriate to seek legal advice that any proposed letter is suitable.

To the appropriate representative of those charged with governance of ABC Charity:⁸⁵

[The objective and scope of the audit]

You⁸⁶ have requested that we audit the [financial report/ performance report] of [ABC Charity (the “entity”)], which comprise the financial statements, and the service performance information [, and entity information]. The complete set of financial statements comprise the statement of financial position as at December 31, 20XX, [the statement of comprehensive revenue and expense, statement of financial performance, statement of changes in net assets/equity], and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory notes. We are pleased to confirm our acceptance and our understanding of this audit engagement by means of this letter.

The objectives of our audit are to obtain reasonable assurance about whether the [financial report/ performance report] as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this [financial report/ performance report].

[The responsibilities of the auditor]

We will conduct our audit in accordance with the ISA (NZ) for LCE. The ISA (NZ) for LCE requires that we comply with ethical requirements. As part of an audit in accordance with the ISA (NZ) for LCE, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the [financial report/ performance report], whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

⁸⁵ The addressees and references in the letter would be those that are appropriate in the circumstances of the engagement, including the relevant jurisdiction.

⁸⁶ Throughout this letter, references to “you,” “we,” “us,” “management,” “those charged with governance” and “auditor” would be used or amended as appropriate in the circumstances.

- Understand internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the [financial report/ performance report] that we have identified during the audit.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by [management and those charged with governance].
- Obtain an understanding of the process applied by the entity to select its elements/aspects of service performance, performance measures and/or descriptions and the measurement bases or evaluation methods.
- Evaluate whether the selection of elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods present an appropriate and meaningful assessment of the entity's service performance in accordance with [the applicable financial reporting framework].
- Evaluate whether the service performance information is prepared in accordance with the entity's measurement bases or evaluation methods, in accordance with the applicable financial reporting framework.
- Conclude on the appropriateness of [those charged with governance's] use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the [financial report/ performance report] or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the [financial report/ performance report], including the disclosures, and whether the [financial report/ performance report] represents the underlying transactions and events in a manner that achieves fair presentation.

Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with the ISA (NZ) for LCE.

[The responsibilities of those charged with governance and identification of the applicable financial reporting framework]⁸⁷

Our audit will be conducted on the basis that [those charged with governance]⁸⁸ acknowledge and understand that they have responsibility on behalf of the entity:

- For the preparation [and fair presentation] of the [financial report/ performance report] in accordance with [applicable financial reporting framework];⁸⁹
- For the selection of elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods that present service performance

⁸⁷ For purposes of this illustrative engagement letter, it is assumed that the auditor has not determined that the law or regulation prescribes those responsibilities in appropriate terms; the descriptions in paragraph 4.2.1(b) of this standard are therefore used)

⁸⁸ Use terminology as appropriate in the circumstances.

⁸⁹ Or, if appropriate, "For the preparation of a [financial report/ performance report] that give a true and fair view in accordance with [applicable financial reporting framework]"

information that is appropriate and meaningful in accordance with the applicable financial reporting framework;

- For the preparation and fair presentation of service performance information in accordance with the entity's measurement bases or evaluation methods, in accordance with the applicable financial reporting framework;
- For the overall presentation, structure and content of the service performance information in accordance with the applicable financial reporting framework;
- For such internal control as [they] determine is necessary to enable the preparation of a [financial report/ performance report] that are free from material misstatement, whether due to fraud or error; and
- To provide us with:
 - (i) Access to all information of which [management and those charged with governance] is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
 - (ii) Additional information that we may request from [management and those charged with governance] for the purpose of the audit; and
 - (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

As part of our audit process, we will request from [those charged with governance], written confirmation concerning representations made to us in connection with the audit.

We look forward to full cooperation from your staff during our audit.

[Other relevant information]

[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]

[Reporting]

[Insert appropriate reference to the expected form and content of the auditor's report including, if applicable, the reporting on other information.]

The form and content of our report may need to be amended in the light of our audit findings.

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of the [financial report/ performance report] including our respective responsibilities.

XYZ & Co.

Acknowledged and agreed on behalf of ABC Charity by

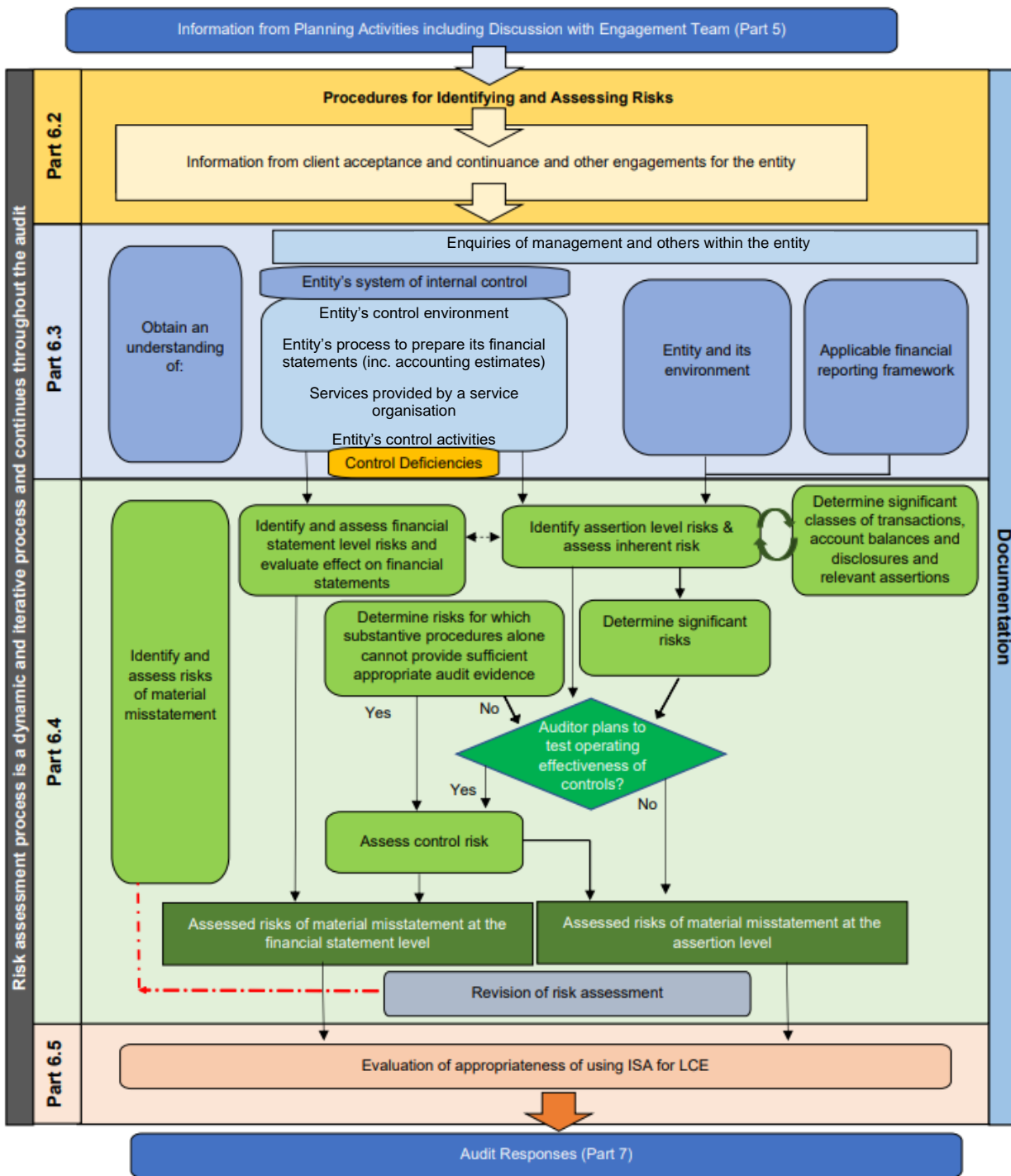
(signed)

.....

Name and Title

Date

Identifying and Assessing the Risks of Material Misstatement (Part 6)



Fraud Risk Factors

The fraud risk factors set out below are examples of factors that may be faced by auditors during an audit of less complex entities. Examples are separately presented for the two types of fraud – fraudulent financial reporting and misappropriation of assets.

The risk factors are further classified based on the three conditions generally present when material misstatements due to fraud occur: (a) incentives/pressures, (b) opportunities, and (c) attitudes/rationalizations. Although the risk factors cover a broad range of situations, they are only examples and, accordingly, the auditor may identify additional or different risk factors. Not all of these examples are relevant in all circumstances, and some may be of greater or lesser significance in entities of different sizes or with different ownership characteristics or circumstances. Also, the order of the examples risk factors provided is not intended to reflect their relative importance or frequency of occurrence.

Risk Factors Relating to Misstatements Arising from Fraudulent Financial Reporting

The following are examples of risk factors relating to misstatements arising from fraudulent financial reporting.

Incentives/Pressures

Financial stability or profitability is threatened by economic, industry, or entity operating conditions, such as (or as indicated by):

- Significant declines in customer demand or increasing business failures in the industry or overall economy.
- High degree of competition or market saturation, accompanied by declining margins.
- Operating losses causing the threat of bankruptcy or foreclosure.
- Recurring negative cash flows from operations or an inability to generate cash flows from operations.

Pressure exists for management to meet the requirements or expectations of third parties due to:

- Pressure to renew, or obtain additional, financing, or to meet debt repayment or debt covenant requirements and therefore to overstate performance or position in order to demonstrate profitability and long-term viability.
- Pressure to understate revenue in order to reduce tax liabilities.

Opportunities

Opportunities to engage in fraudulent financial reporting that can arise from the following:

- Related-party transactions not in the ordinary course of business or with related entities not audited or audited by another firm.
- The domination of management by a single person or small group (in a non owner-managed business) without compensating controls.
- The system of internal control is deficient as a result of the following:
 - Limited segregation of duties or anti-fraud controls (e.g., fraud hotlines)

- Inadequate involvement of management in operations or other activities that may help management to prevent or detect misstatements in accounting information, or to identify controls that are not operating as intended.
- Accounting and information systems that are not effective, including situations involving significant deficiencies in internal control.

Attitudes/Rationalizations

- Poor communication, implementation, support, or enforcement of the entity's values or ethical standards by management, or the communication of inappropriate values or ethical standards.
- The owner-manager makes no distinction between personal and business transactions.
- Dispute between shareholders in a closely held entity.
- Recurring attempts by management or owners to justify marginal or inappropriate accounting on the basis of materiality or to help the company survive.
- The relationship between management and the current or predecessor auditor is strained by disputes, unreasonable demands on the auditor, restrictions on access to people or information, or domineering management ~~behavior~~ behaviour.

Risk Factors Arising from Misstatements Arising from Misappropriation of Assets

Some of the risk factors related to misstatements arising from fraudulent financial reporting may also be present when misstatements arising from misappropriation of assets occur, which often is a common fraud in less complex entities. For example, deficiencies in internal control may be present when misstatements due to either fraudulent financial reporting or misappropriation of assets exist. The following are examples of risk factors related to misstatements arising from misappropriation of assets.

Incentives/Pressures

- Personal financial obligations may create pressure on management or employees with access to cash or other assets susceptible to theft to misappropriate those assets.
- Adverse relationships between the entity and employees with access to cash or other assets susceptible to theft may motivate those employees to misappropriate those assets. For example:
- Known or anticipated future employee layoffs.
- Recent or anticipated changes to employee compensation or benefit plans.
- Promotions, compensation, or other rewards inconsistent with expectations.

Opportunities

Certain characteristics or circumstances may increase the susceptibility of assets to misappropriation:

- Large amounts of cash on hand or processed.
- Inventory items that are small in size, of high value, or in high demand.
- Fixed assets which are small in size, marketable, or lacking observable identification of ownership.

Inadequate internal control over assets may increase the susceptibility of misappropriation of those assets. For example, misappropriation of assets may occur because there is the following:

- Inadequate segregation of duties or independent checks.
- Inadequate system of authorization and approval of transactions (for example, in purchasing).

- Inadequate record keeping or physical safeguards over cash, inventory, or fixed assets.
- Lack of mandatory vacations for employees performing key control functions.
- Inadequate management understanding of information technology.

Attitudes/Rationalizations

- Disregard for the need for monitoring or reducing risks related to misappropriations of assets.
- Disregard for internal control by overriding existing controls or failing to take appropriate remedial action on known misappropriations, including petty theft.
- ~~Behavior~~Behaviour indicating displeasure or dissatisfaction with the entity or its treatment of the employee.

Assertions

In identifying and assessing the risks of material misstatement, the auditor of less complex entities (LCEs) may use the categories of assertions as described below or may express them differently provided all aspects described below have been covered. The auditor may choose to combine the assertions about classes of transactions and events, and related disclosures, with the assertions about account balances, and related disclosures.

An auditor of an LCE may use the following assertions in considering the different types of potential misstatements that may occur. The assertions may fall into the following categories:

Assertions About Classes of Transactions and Events, and Related Disclosures, For the Period Under Audit

- Occurrence—transactions and events that have been recorded or disclosed have occurred, and such transactions and events pertain to the entity.
- Completeness—all transactions and events that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
- Accuracy—amounts and other data relating to recorded transactions and events have been recorded appropriately, and related disclosures have been appropriately measured and described.
- Cutoff—transactions and events have been recorded in the correct accounting period.
- Classification—transactions and events have been recorded in the proper accounts.
- Presentation—transactions and events are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.

Assertions About Account Balances, and Related Disclosures, At the Period End

- Existence—assets, liabilities and equity interests exist.
- Rights and obligations—the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
- Completeness—all assets, liabilities and equity interests that should have been recorded have been recorded, and all related disclosures that should have been included in the financial statements have been included.
- Accuracy, valuation and allocation—assets, liabilities and equity interests have been included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments have been appropriately recorded, and related disclosures have been appropriately measured and described.
- Classification—assets, liabilities and equity interests have been recorded in the proper accounts.
- Presentation—assets, liabilities and equity interests are appropriately aggregated or disaggregated and clearly described, and related disclosures are relevant and understandable in the context of the requirements of the applicable financial reporting framework.

The assertions described above, adapted as appropriate, may also be used by the auditor in considering the different types of misstatements that may occur in disclosures not directly related to recorded classes of transactions, events or account balances.

[NZ] Assertions about Service Performance Information (when applying Part 11)

Assertions used by the auditor in considering the different types of potential misstatements of service performance information that may occur may fall into the following categories:

- Occurrence—service performance that has been reported has occurred.
- Attributable to the entity—the service performance reported by the entity includes only service performance that the entity has evidence to support its involvement with either directly or in conjunction with other entities with common goals.
- Completeness—all important service performance that should have been reported has been included in the service performance information.
- Accuracy—service performance has been reported, measured and described appropriately and is not inconsistent with the financial statement information.
- Cut-off—service performance has been reported in the correct period.
- Presentation—service performance is appropriately aggregated or disaggregated, clearly displayed and not misleading, and related disclosures are relevant and understandable.

The auditor may use the assertions as described above or may express them differently provided all aspects described above have been covered. For example, the auditor may choose to combine the assertions about occurrence and attribution or based on the nature of the service performance information reported consider existence may be more appropriate than occurrence.

APPENDIX 6

Examples of Factors Influencing Sample Size for Tests of Controls and Test of Details

The following are factors that the auditor may consider when determining the sample size for tests of controls. These factors, which need to be considered together, assume the auditor does not modify the nature or timing of tests of controls or otherwise modify the approach to substantive procedures in response to assessed risks.

Factor Influencing Sample Size for Tests of Controls	Effect on sample size
An increase in the extent to which the auditor's risk assessment takes into account plans to test the operating of effectiveness of controls	Increase
An increase in the tolerable rate of deviation	Decrease
An increase in the expected rate of deviation of the population to be tested	Increase
An increase in the auditor's desired level of assurance that the tolerable rate of deviation is not exceeded by the actual rate of deviation in the population	Increase
An increase in the number of sampling units in the population	Negligible effect

The following are factors that the auditor may consider when determining the sample size for tests of details. These factors, which need to be considered together, assume the auditor does not modify the approach to tests of controls or otherwise modify the nature or timing of substantive procedures in response to the assessed risks.

Factor Influencing Sample Size for Tests of Details	Effect on sample size
An increase in the auditor's assessment of the risk of material misstatement	Increase
An increase in the use of other substantive procedures directed at the same assertion	Decrease
An increase in the auditor's desired level of assurance that tolerable misstatement is not exceeded by actual misstatement in the population	Increase
An increase in tolerable misstatement	Decrease
An increase in the amount of misstatement the auditor expects to find in the population	Increase
Stratification of the population when appropriate	Decrease
The number of sampling units in the population	Negligible effect

Illustrative Representation Letter

The following illustrative letter includes written representations that are required by Part 8.6 of the ~~ISA for LCE~~ISA (NZ) for LCE. It is assumed in this illustration that the requirement to obtain a written representation relating to going concern is not relevant; and that there are no exceptions to the requested written representations. If there were exceptions, the representations would need to be modified to reflect the exceptions.

(Entity Letterhead)

(To Auditor) _____ (Date) _____

~~(Date)~~

This representation letter is provided in connection with your audit of the financial statements of [ABC Company (the "entity")], for the year ended December 31, 20XX for the purpose of expressing an opinion as to whether the financial statements are presented fairly, in all material respects, (or *give a true and fair view*) in accordance with [the applicable financial reporting framework] issued by the New Zealand Accounting Standards Board.

We confirm that (, to the best of our knowledge and belief, having made such enquiries as we considered necessary for the purpose of appropriately informing ourselves):

Financial Statements

- We have fulfilled our responsibilities on behalf of the entity, as set out in the terms of the audit engagement dated [insert date], for the preparation of the financial statements in accordance with [applicable financial reporting framework]; in particular the financial statements are fairly presented (or give a true and fair view) in accordance therewith.
- The methods, the data, and the significant assumptions used in making accounting estimates, and their related disclosures are appropriate to achieve recognition, measurement or disclosure that is reasonable in the context of the applicable financial reporting framework.
- Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of [applicable financial reporting framework].
- All events subsequent to the date of the financial statements and for which [applicable financial reporting framework] require adjustment or disclosure have been adjusted or disclosed.
- The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial statements as a whole. A list of the uncorrected misstatements is attached to the representation letter.
- Any actual or possible litigation and claims whose effects should be considered when preparing the financial statements are accounted for and disclosed in accordance with the applicable financial reporting framework.
- [Any other matters that the auditor may consider appropriate.]

Information Provided

- We have provided you with:
 - Access to all information of which we are aware that is relevant to the preparation of the financial statements, such as records, documentation and other matters;
 - Additional information that you have requested from us for the purpose of the audit; and
 - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
- All transactions have been recorded in the accounting records and are reflected in the financial statements.
- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity and involves:
 - Management;
 - Employees who have significant roles in internal control; or
 - Others where the fraud could have a material effect on the financial statements.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.
- We have disclosed to you all known instances of non-compliance or suspected non-compliance with law or regulation whose effects should be considered when preparing financial statements.
- We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.
- We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware.
- [Any other matters that the auditor may consider necessary.]

Management _____ Management

Signed on behalf of [Those Charged with Governance] of [ABC Company] by:

(signed)

.....

Name and Title

(signed)

.....

Name and Title

[NZ] APPENDIX 7A**Illustrative Representation Letter including Service Performance Information⁹⁰**

The following illustrative letter includes written representations that are required by Part 11.11. and Part 8.6. of the ISA (NZ) for LCE. It is assumed in this illustration that the applicable financial reporting framework is a fair presentation framework, that the requirement to obtain a written representation relating to going concern is not relevant; and that there are no exceptions to the requested written representations. If there were exceptions, the representations would need to be modified to reflect the exceptions.

(Entity Letterhead)

(To Auditor)

(Date)

This representation letter is provided in connection with your audit of the [financial report/ performance report] of [ABC Entity (the "entity")], for the year ended December 31, 20XX which comprise the financial statements, and the service performance information [, and entity information], for the purpose of expressing an opinion as to whether the [financial report/ performance report] presents fairly, in all material respects, (or gives a true and fair view of):

- [the entity information as at December 31, 20XX; and]
- the financial position of the entity as at December 31, 20XX, and its financial performance, and its cash flows for the year then ended; and
- the service performance for the year ended December 31, 20XX in that the service performance information is appropriate and meaningful and prepared in accordance with the entity's measurement bases or evaluation methods

in accordance with [the applicable financial reporting framework (e.g.: PBE Standards)] issued by the New Zealand Accounting Standards Board.

We confirm that (, to the best of our knowledge and belief, having made such enquiries as we considered necessary for the purpose of appropriately informing ourselves):

[Financial Report/ Performance Report]

- We have fulfilled our responsibilities on behalf of the entity, as set out in the terms of the audit engagement dated [insert date], for:
 - The preparation of the [financial report/ performance report] in accordance with the [applicable financial reporting framework]; in particular the [financial report/ performance report] is fairly presented (or give a true and fair view) in accordance therewith.
 - The selection of elements/aspects of service performance, performance measures and/or descriptions and measurement bases or evaluation methods that present service performance information that is appropriate and meaningful in accordance with the [applicable financial reporting framework];
 - The preparation of service performance information in accordance with the entity's measurement bases or evaluation methods in accordance with the [applicable financial reporting framework]; and
 - The overall presentation structure and content of the service performance information in accordance with the [applicable financial reporting framework].

⁹⁰ May also be referred to as the Statement of Service Performance.

- The methods, the data, and the significant assumptions used in making accounting estimates, and their related disclosures are appropriate to achieve recognition, measurement or disclosure that is reasonable in the context of the applicable financial reporting framework.
- Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of [applicable financial reporting framework].
- All events subsequent to the date of the financial statements and for which [applicable financial reporting framework] require adjustment or disclosure have been adjusted or disclosed.
- The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the [financial report/ performance report] as a whole. A list of the uncorrected misstatements is attached to the representation letter.
- Any actual or possible litigation and claims whose effects should be considered when preparing the financial statements are accounted for and disclosed in accordance with the applicable financial reporting framework.
- [Any other matters that the auditor may consider appropriate.]

Information Provided

- We have provided you with:
 - Access to all information of which we are aware that is relevant to the preparation of the [financial report/ performance report], such as records, documentation and other matters;
 - Additional information that you have requested from us for the purpose of the audit; and
 - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
- All transactions have been recorded in the accounting records and are reflected in the [financial report/ performance report].
- We have disclosed to you the results of our assessment of the risk that the [financial report/ performance report] may be materially misstated as a result of fraud.
- We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity and involves:
 - Management;
 - Employees who have significant roles in internal control; or
 - Others where the fraud could have a material effect on the [financial report/ performance report].
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's [financial report/ performance report] communicated by employees, former employees, analysts, regulators or others.
- We have disclosed to you all known instances of non-compliance or suspected non-compliance with law or regulation whose effects should be considered when preparing a [financial report/ performance report].
- We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the [financial report/ performance report].
- We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware.

- [Any other matters that the auditor may consider necessary.]

Signed on behalf of [Those Charged with Governance] of [ABC Charity] by:

(signed)

(signed)

.....

.....

Name and Title

Name and Title

CONFORMING AMENDMENTS ARISING FROM THE ISA FOR LCE ISA (NZ) FOR LCE

Note: The following are conforming amendments to other International assurance Standards as a result of the approval of the ISA for LCE ISA (NZ) for LCE. These amendments will become effective at the same time as the ISA for LCE ISA (NZ) for LCE and are shown with marked changes from the latest approved versions of the International assurance Standards that are amended. The footnote numbers within these amendments do not align with the International Standards assurance standards that are amended, and reference should be made to those International assurance Standards.

XR B Au1 APPLICATION OF AUDITING AND ASSURANCE STANDARDS

APPENDIX 2B

INTERNATIONAL STANDARDS ON AUDITING (NEW ZEALAND) FOR AUDITS OF FINANCIAL STATEMENTS OF LESS COMPLEX ENTITIES

This appendix is an integral part of the Standard

This appendix lists the standard to be applied in conducting an audit of historical financial information of a Less Complex Entity.

The XR B permits the voluntary application of the ISA (NZ) for LCE in specific circumstances. This audit practitioners may voluntarily adopt this standard:

(a) On or after the mandatory date, or early adoption accounting period, as defined in the Commencement and Application section of the ISA (NZ) for LCE standard; and

(b) The auditor determines that the audit engagement can be undertaken using the ISA (NZ) for LCE in accordance with Part A of the ISA (NZ) for LCE.

ISA (NZ) for LCE International Standards on Auditing (New Zealand) for audits of financial statements of less complex entities

...

APPENDIX 6

[ISA (NZ) for LCE to be added to the diagram: Overview of the Auditing and Assurance Standards of the XR B, and the Engagements Governed by the Standards.]

...

**PES 1, INTERNATIONAL CODE OF ETHICS FOR ASSURANCE
PRACTITIONERS (INCLUDING INTERNATIONAL INDEPENDENCE
STANDARDS) (NEW ZEALAND)**

...

SECTION 400

**APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW
ENGAGEMENTS**

...

400.4 Professional and Ethical Standard 3⁹¹ requires a firm to design, implement and operate a system of quality management for audits or reviews of financial statements performed by the firm. As part of this system of quality management, Professional and Ethical Standard 3 requires the firm to establish quality objectives that address the fulfilment of responsibilities in accordance with relevant ethical requirements including those related to independence. Under Professional and Ethical Standard 3, relevant ethical requirements are those related to the firm, its personnel and, when applicable, others subject to independence the requirements to which the firm and the firm's engagements are subject. International Standards on Auditing (New Zealand), International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE), International Standards on Review Engagements (New Zealand) and New Zealand Standards on Review Engagements establish responsibilities for engagement partners and engagement teams at the level of the engagement for audits and reviews, respectively. The allocation of responsibilities within a firm will depend on its size, structure and organisation. Many of the provisions of this Part do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to "firm" for ease of reference. A firm assigns operational responsibility for compliance with independence requirements to an individual(s) in accordance with Professional and Ethical Standard 3. In addition, an individual assurance practitioner remains responsible for compliance with any provisions that apply to that assurance practitioner's activities, interests or relationships.

...

SECTION 900

**APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR ASSURANCE
ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS**

...

900.3 Professional and Ethical Standard 3 requires a firm to design, implement and operate a system of quality management for assurance engagements performed by the firm. As part of this system of quality management, Professional and Ethical Standard 3 requires the firm to establish quality objectives that address the fulfilment of responsibilities in accordance with relevant ethical requirements, including those related to independence. Under Professional and Ethical Standard 3, relevant ethical requirements are those related to the firm, its personnel and, when applicable, others subject to the independence requirements to which the firm and the firm's engagements

⁹¹ Professional and Ethical Standard 3, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

~~are subject. In addition, International Standards on Assurance Engagements (New Zealand), Standards on Assurance Engagements, International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE) and International Standards on Auditing (New Zealand) establish responsibilities for engagement partners and engagement teams at the level of the engagement. The allocation of responsibilities within a firm will depend on its size, structure and organisation. Many of the provisions of Part 4B do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to “firm” for ease of reference. A firm assigns operational responsibility for compliance with independence requirements to an individual(s) in accordance with Professional and Ethical Standard 3. Additionally, an individual assurance practitioner remains responsible for compliance with any provisions that apply to that assurance practitioner’s activities, interests or relationships.~~

...

GLOSSARY

...

Assurance engagement ~~An engagement in which an assurance practitioner aims to obtain sufficient appropriate evidence in or to express a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the subject matter information (that is, the outcome of the measurement or evaluation of an underlying subject matter against criteria).~~

~~(ISAE (NZ) 3000 (Revised) describes the elements and objectives of an assurance engagement conducted under that Standard and Explanatory Guide (EG) Au1 *Overview of Auditing and Assurance Standards* provides a general description of assurance engagements to which International Standards on Auditing (New Zealand) (ISAs (NZ)), International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE), International Standards on Review Engagements (New Zealand) (ISREs (NZ)), New Zealand Standard on Review Engagements (NZ SRE), International Standards on Assurance Engagements (New Zealand) (ISAEs (NZ)), and Standards on Assurance Engagements (SAEs) apply.)~~

~~*In Part 4B, the term ‘assurance engagement’ refers to assurance engagements that are not audit or review engagements.*~~

Audit engagement ~~A reasonable assurance engagement in which an assurance practitioner expresses an opinion whether financial statements are prepared, in all material respects (or give a true and fair view or are presented fairly, in all material respects), in accordance with an applicable financial reporting framework, such as an engagement conducted in accordance with International Standards on Auditing (New Zealand) or International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE). This includes a Statutory Audit, which is an audit required by legislation or other regulation.~~

~~PREFACE TO THE INTERNATIONAL QUALITY MANAGEMENT, AUDITING, REVIEW, OTHER ASSURANCE AND RELATED SERVICES PRONOUNCEMENTS~~

...

~~The Authority Attaching to International Standards Issued by the International Auditing and Assurance Standards Board~~

5. ~~International standards to be applied in the audit of historical financial information are:~~

~~(a) International Standards on Auditing (ISAs); or~~

~~(b) The International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE), which may only be applied in accordance with the preface and the authority set out in the ISA for LCE.~~

...

9. ~~ISAs, the ISA for LCE, ISREs, ISAEs, and ISRSs are collectively referred to as the IAASB's Engagement Standards.~~

...

~~The International Standard on Auditing for Audits of Financial Statements of Less Complex Entities~~

11A. ~~The ISA for LCE is written in the context of an audit of financial statements of a less complex entity by an independent auditor. The authority of the ISA for LCE is set out in the Preface and Part A of the standard.~~

...

~~Non-Authoritative Material~~

...

~~International Auditing Practice Notes~~

21. ~~International Auditing Practice Notes (IAPNs) do not impose additional requirements on auditors beyond those included in the ISAs or the ISA for LCE, nor do they change the auditor's responsibility to comply with all ISAs, or the ISA for LCE, relevant to the audit. IAPNs provide practical assistance to auditors. They are intended to be disseminated by those responsible for national standards, or used in developing corresponding national material. They also provide material that firms can use in developing their training programs and internal guidance.~~

...

PES 3ISQM-1, QUALITY MANAGEMENT FOR FIRMS THAT PERFORM AUDITS OR REVIEWS OF FINANCIAL STATEMENTS, OR OTHER ASSURANCE OR RELATED SERVICES ENGAGEMENTS

...

Application and Other Explanatory Material

Scope of this ISQM-Professional and Ethical Standard (Ref: Para. 3–4)

A1. Other pronouncements of the IAASBNZAuASB, including the International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)ISA (NZ) for LCE, ISRE

~~(NZ) 2400–(Revised)~~⁹² and ISAE ~~(NZ) 3000 (Revised)~~,⁹³ also establish requirements for the engagement partner for the management of quality at the engagement level.

...

Authority of this ~~ISQM-Professional and Ethical Standard~~ (Ref: Para. 12)

...

A8. Where necessary, the application and other explanatory material provides further explanation of the requirements and guidance for carrying them out. In particular, it may:

- Explain more precisely what a requirement means or is intended to cover; and
- Include examples that illustrate how the requirements might be applied.

While such guidance does not in itself impose a requirement, it is relevant to the proper application of the requirements. The application and other explanatory material may also provide background information on matters addressed in this ~~ISQMPES~~. ~~In certain instances, references are included to individual ISAs. If the audit engagement is conducted in accordance with the ISA for LCEISA (NZ) for LCE, the ISA for LCEISA (NZ) for LCE may also address related matters in the context of an audit of the financial statements of a less complex entity but these are not referenced in this ISQMPES.~~ Where appropriate, additional considerations specific to public sector audit ~~organization~~~~organisation~~ are included within the application and other explanatory material. These additional considerations assist in the application of the requirements in this ~~ISQMPES~~. They do not, however, limit or reduce the responsibility of the firm to apply and comply with the requirements in this ~~ISQMPES~~.

...

Engagement Performance

...

Engagement Documentation (Ref: Para. 31(f))

A83. Law, regulation or professional standards may prescribe the time limits by which the assembly of final engagement files for specific types of engagements are to be completed. Where no such time limits are prescribed in law or regulation, the time limit may be determined by the firm. In the case of engagements conducted under the ISAs ~~(NZ)~~, the ~~ISA for LCEISA (NZ) for LCE~~ or ISAEs ~~(NZ) or SAEs~~, an appropriate time limit within which to complete the assembly of the final engagement file is ordinarily not more than 60 days after the date of the engagement report.

...

A85. Law, regulation or professional standards may prescribe the retention periods for engagement documentation. If the retention periods are not prescribed, the firm may consider the nature of the engagements performed by the firm and the firm's circumstances, including whether the engagement documentation is needed to provide a record of matters of continuing significance to future engagements. In the case of engagements conducted under the ISAs, the ~~ISA for LCEISA (NZ) for LCE~~ or ISAEs ~~or SAEs~~, the retention period is ordinarily no shorter than five years from the date of the engagement report, or, if later, the date of the auditor's report on the group financial statements, when applicable.

⁹² International Standard on Review Engagements (ISRE) (NZ) 2400, *Engagements to Review Historical Financial Statements*

⁹³ International Standard on Assurance Engagements (ISAE) (NZ) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

...

~~ISQM 2~~PES 4, ENGAGEMENT QUALITY REVIEWS

Introduction

...

Authority of this ~~ISQM~~Professional and Ethical Standard

10. This ~~ISQM-PES~~ contains the objective for the firm in following this ~~PES~~~~ISQM~~, and requirements designed to enable the firm and the engagement quality reviewer to meet that stated objective. In addition, this ~~PES~~ ~~ISQM~~ contains related guidance in the form of application and other explanatory material and introductory material that provides context relevant to a proper understanding of this ~~PES~~~~ISQM~~, and definitions. ~~PES 3~~⁹⁴~~ISQM 1~~ explains the terms objective, requirements, application and other explanatory material, introductory material, and definitions. (Ref: Para. A0A)

...

Application and Other Explanatory Material

Authority of this ~~ISQM~~Professional and Ethical Standard (Ref: Para. 10)

A0A. The application and other explanatory material may also provide background information on matters addressed in this ~~ISQM~~PES. In certain instances, references are included to individual International Standards on Auditing ~~New Zealand~~ (ISAs (NZ)). If the audit engagement is conducted in accordance with the International Standard on Auditing (~~New Zealand~~) for Audits of Financial Statements of Less Complex Entities (~~ISA for LCE~~ISA (NZ) for LCE), the ~~ISA for LCE~~ISA (NZ) for LCE may also address related matters in the context of an audit of the financial statements of a less complex entity but these are not referenced in this ~~ISQM~~PES.

...

Performance of the Engagement Quality Review (Ref: Para. 24–27)

Engagement Partner Responsibilities in Relation to the Engagement Quality Review (Ref: Para. 24(b))

- A25. ISA 220 ~~(NZ)~~ (Revised)⁹⁵ establishes the requirements for the engagement partner in audit engagements for which an engagement quality review is required, including:
- Determining that an engagement quality reviewer has been appointed;
 - Cooperating with the engagement quality reviewer and informing other members of the engagement team of their responsibility to do so;
 - Discussing significant matters and significant ~~judgment~~judgements arising during the audit engagement, including those identified during the engagement quality review, with the engagement quality reviewer; and
 - Not dating the auditor's report until the completion of the engagement quality review.

...

⁹⁴ PES 3, paragraph 14

⁹⁵ ~~International Standard on Auditing (ISA (NZ))~~ 220 (Revised), *Quality Management for an Audit of Financial Statements*, paragraph 36

ISAE (NZ) 3000 (REVISED), ASSURANCE ENGAGEMENTS OTHER THAN AUDITS OR REVIEWS OF HISTORICAL FINANCIAL INFORMATION

Introduction

1. This International Standard on Assurance Engagements (~~New Zealand~~) (ISAE (NZ)) deals with assurance engagements other than audits or reviews of historical financial information, ~~which Audits of historical financial information are dealt with in International Standards on Auditing (New Zealand) (ISAs (NZ)) and the International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (ISA for LCE)ISA (NZ) for LCE), and reviews of historical financial information are dealt with in International Standards on Review Engagements (New Zealand) (ISREs (NZ)), respectively. (Ref: Para. A21–A22)~~

...

~~ISRE (NZ) 2400 (REVISED), REVIEW OF HISTORICAL FINANCIAL STATEMENTS PERFORMED BY AN ASSURANCE PRACTITIONER WHO IS NOT THE AUDITOR OF THE ENTITY~~ENGAGEMENTS TO REVIEW HISTORICAL FINANCIAL STATEMENTS

...

Requirements

...

The Assurance Practitioner's Report

86. The assurance practitioner's report for the review engagement shall be in writing, and shall contain the following elements: (Ref: Para. A12~~24~~–A12~~57~~, A14~~86~~, A15~~480~~)

...

- (g) A description of a review of financial statements and its limitations, and the following statements: (Ref: Para. A13~~24~~)
- (i) A review engagement under this ISRE (NZ) is a limited assurance engagement;
 - (ii) The assurance practitioner performs procedures, primarily consisting of making einquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained; and
 - (iii) The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with auditing standards issued by the International Auditing and Assurance Standards External Reporting Board International Standards on Auditing (New Zealand) (ISAs (NZ)) and, accordingly, the practitioner does not express an audit opinion on the financial statements;

...

Appendix 2

...

Illustration 1

...

Assurance Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying financial statements. We conducted our review in accordance with International Standard on Review Engagements ~~(New Zealand)~~ (ISRE ~~(NZ)~~ 2400 ~~(Revised)~~, ~~Review of Historical Financial Statements Performed by an Assurance Practitioner who is not the Auditor of the Entity. Engagements to Review Historical Financial Statements.~~ ISRE ~~(NZ)~~ 2400 ~~(Revised)~~ requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of financial statements in accordance with ISRE ~~(NZ)~~ 2400 ~~(Revised)~~ is a limited assurance engagement. The ~~assurance~~ practitioner performs procedures, primarily consisting of making ~~e~~inquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with ~~auditing standards issued by the International Auditing and Assurance Standards External Reporting Board International Standards on Auditing (New Zealand)~~. Accordingly, we do not express an audit opinion on these financial statements.

...

Illustration 2

...

~~Assurance~~ Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying financial statements. We conducted our review in accordance with International Standard on Review Engagements ~~(New Zealand)~~ (ISRE ~~(NZ)~~ 2400 ~~(Revised)~~, ~~Engagements to Review Historical Financial Statements~~ ~~Review of Historical Financial Statements Performed by an Assurance Practitioner who is not the Auditor of the Entity~~. ISRE ~~(NZ)~~ 2400 ~~(Revised)~~ requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of financial statements in accordance with ISRE ~~(NZ)~~ 2400 ~~(Revised)~~ is a limited assurance engagement. The ~~assurance~~ practitioner performs procedures, primarily consisting of making ~~e~~inquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with ~~auditing standards issued by the International Auditing and Assurance Standards External Reporting Board International Standards on Auditing (New Zealand)~~. Accordingly, we do not express an audit opinion on these financial statements.

...

Illustration 3

...

~~Assurance~~ Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying financial statements. We conducted our review in accordance with International Standard on Review Engagements ~~(New Zealand)~~ (ISRE ~~(NZ)~~ 2400 ~~(Revised)~~, ~~Review of Historical Financial Statements Performed by an Assurance~~

~~*Practitioner who is not the Auditor of the Entity Engagements to Review Historical Financial Statements.*~~ ISRE (NZ) 2400 ~~(Revised)~~ requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of financial statements in accordance with ISRE (NZ) 2400 ~~(Revised)~~ is a limited assurance engagement. The assurance practitioner performs procedures, primarily consisting of making enquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with auditing standards issued by the ~~International Auditing and Assurance Standards~~ External Reporting Board ~~International Standards on Auditing (New Zealand)~~. Accordingly, we do not express an audit opinion on these financial statements.

...

Illustration 4

...

Assurance Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying consolidated financial statements. We conducted our review in accordance with International Standard on Review Engagements (New Zealand) (ISRE (NZ)) 2400 ~~(Revised)~~, ~~*Review of Historical Financial Statements Performed by an Assurance Practitioner who is not the Auditor of the Entity Engagements to Review Historical Financial Statements.*~~ ISRE (NZ) 2400 ~~(Revised)~~ requires us to conclude whether anything has come to our attention that causes us to believe that the consolidated financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of consolidated financial statements in accordance with ISRE (NZ) 2400 ~~(Revised)~~ is a limited assurance engagement. The assurance practitioner performs procedures, primarily consisting of making enquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with auditing standards issued by the ~~International Auditing and Assurance Standards~~ External Reporting Board ~~International Standards on Auditing (New Zealand)~~. Accordingly, we do not express an audit opinion on these consolidated financial statements.

...

Illustration 6

...

Assurance Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying financial statements. We conducted our review in accordance with International Standard on Review Engagements (New Zealand) (ISRE (NZ)) 2400 ~~(Revised)~~, ~~*Review of Historical Financial Statements Performed by an Assurance Practitioner who is not the Auditor of the Entity Engagements to Review Historical Financial Statements.*~~ ISRE (NZ) 2400 ~~(Revised)~~ requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material

respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of financial statements in accordance with ISRE (NZ) 2400 (Revised) is a limited assurance engagement. The assurance practitioner performs procedures, primarily consisting of making enquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with auditing standards issued by the ~~International Auditing and Assurance Standards Board~~ International Standards on Auditing (New Zealand). Accordingly, we do not express an audit opinion on these financial statements.

...

Illustration 7

...

Assurance Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying financial statement. We conducted our review in accordance with International Standard on Review Engagements (New Zealand) (ISRE (NZ) 2400 (Revised), *Review of Historical Financial Statements Performed by an Assurance Practitioner who is not the Auditor of the Entity*~~Engagements to Review Historical Financial Statements~~. ISRE (NZ) 2400 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that the financial statement is not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of financial statements in accordance with ISRE 2400 (Revised) is a limited assurance engagement. The assurance practitioner performs procedures, primarily consisting of making enquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with auditing standards issued by the ~~International Auditing and Assurance Standards Board~~ International Standards on Auditing (New Zealand). Accordingly, we do not express an audit opinion on this financial statement.

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INTERNATIONAL FRAMEWORK FOR ASSURANCE ENGAGEMENTS

Introduction

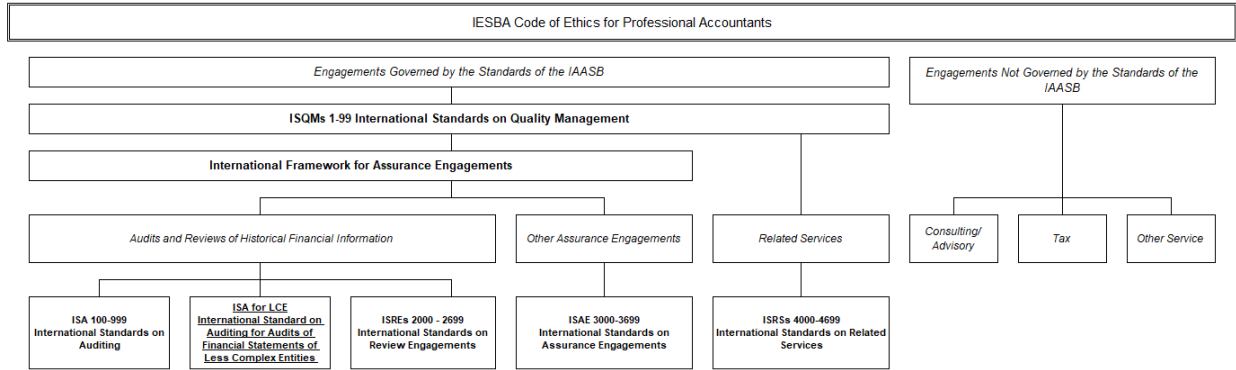
- ~~This Framework is issued solely to facilitate understanding of the elements and objectives of an assurance engagement and the engagements to which International Standards on Auditing (ISA), the International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE), International Standards on Review Engagements (ISRE) and International Standards on Assurance Engagements (ISAE) (hereinafter referred to as Assurance Standards) apply.~~

...

Appendix 1

Pronouncements Issued by the IAASB, and Their Relationship to Each Other and the IESBA Code

This Appendix illustrates the ambit of pronouncements issued by the IAASB, and their relationship to each other and to the IESBA Code of Ethics for Professional Accountants



~~INTERNATIONAL AUDITING PRACTICE NOTE 1000, SPECIAL CONSIDERATIONS IN AUDITING FINANCIAL INSTRUMENTS~~

~~International Auditing Practice Note (IAPN) 1000, Special Considerations in Auditing Financial Instruments, should be read in conjunction with the Preface to the International Quality Management, Auditing, Review, Other Assurance, and Related Services Pronouncements. IAPNs do not impose additional requirements on auditors beyond those included in the auditing standards issued by the International Auditing and Assurance Standards Board International Standards on Auditing (ISAs), nor do they change the auditor's responsibility to comply with all International Standards on Auditing (ISAs) relevant to the audit or the International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE). IAPNs provide practical assistance to auditors. They are intended to be disseminated by those responsible for national standards, or used in developing corresponding national material. They also provide material that firms can use in developing their training programs and internal guidance.~~

Introduction

...

~~7. An audit in accordance with ISAs or the ISA for LCE is conducted on the premise that management and, where appropriate, those charged with governance have acknowledged certain responsibilities. Such responsibilities subsume making fair value measurements. This IAPN does not impose responsibilities on management or those charged with governance nor override laws and regulation that govern their responsibilities.~~

...

ACCOMPANYING ATTACHMENT: CONFORMITY TO THE INTERNATIONAL STANDARDS ON AUDITING FOR AUDITS OF FINANCIAL STATEMENTS OF LESS COMPLEX ENTITIES

This conformity statement accompanies but is not part of the ISA (NZ) for LCE.

Conformity with International Standards on Auditing for Audits of Financial Statements of Less Complex Entities

This International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities (ISA (NZ) for LCE) conforms to International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE), issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been amended or added to this ISA (NZ) for LCE (and do not appear in the text of the equivalent ISA for LCE), are identified with the prefix "NZ".

This ISA (NZ) for LCE incorporates terminology and definitions used in New Zealand.

Part 11 has been added to this ISA (NZ) for LCE to enable the audit of service performance information. It does not appear in ISA for LCE.

Compliance with this ISA (NZ) for LCE enables compliance with ISA for LCE.

Comparison with Australian Auditing Standards

There is no equivalent Australian Auditing Standard, issued by the Australian Auditing and Assurance Standards Board (AUASB).

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ISA (NZ) for Less Complex Entities

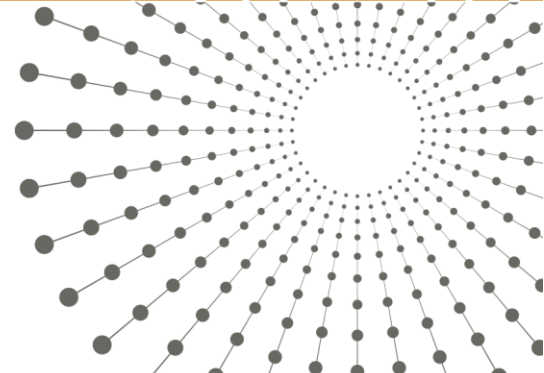
New Zealand adoption of a standard for audits of Less Complex Entities

Consultation document



DATE

Consultation closes DATE





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PART ONE: Introduction





1.

What is this consultation about?

The External Reporting Board has issued this consultation document to seek feedback on:

- **Whether to adopt the International Standard on Auditing (ISA) for Less Complex Entities (LCE) in New Zealand.**
- **The applicability of the standard in New Zealand.**
- **If and how to incorporate service performance information within the New Zealand Standard.**

1. What is the ISA for LCE?

The International Auditing and Assurance Standards Board (IAASB) recently issued a new auditing standard, known as the *International Standard on Auditing for Audits of Financial Statements of Less Complex Entities* (ISA for LCE). The ISA for LCE is a new stand-alone auditing standard available for auditors to use when auditing less complex entities. The standard contains all requirements necessary to obtain reasonable assurance about whether the financial statements of a less complex entity, as a whole, are free from material misstatements, whether due to fraud or error. If adopted in New Zealand, it will be referred to as ISA (NZ) for LCE.

2. Why are we consulting on this?

The type of entities seeking an audit varies considerably from large, listed companies to small charities. New Zealand has many LCEs that have audits of their financial statements, including non-profit organisations such as charities and sports clubs, schools and early childhood centres.

While the current auditing standards (ISA (NZ)) are scalable to suit these audits, we have heard comments that the auditing standards are getting increasingly long and detailed, and that they are largely written in the context of highly regulated, large, listed entities. The XRB has previously explored alternative products for LCEs, while monitoring the development of an international standard tailored to suit the nature and circumstances of audits of LCEs. At this time, we are consulting on whether the ISA for LCE would be suitable for New Zealand.

3. Seeking Your Feedback

This consultation explores whether or not we should adopt the standard, adapted for New Zealand circumstances, and if so, what types of entities the standard should apply to. While the XRB is considering the adoption of the international audit standard, the standard won't be mandated for use. Our questions that we'd like your feedback on are summarised on page 16.



This consultation document should be read in conjunction with the Exposure Draft. We have also produced an 'At a glance' summary of our consultation as well as an Introductory fact sheet – available on the consultation page of our website.



2.

How to provide feedback

Responding to consultation questions

We are seeking comments on the questions raised in this consultation document. We will consider all comments received.

Please feel free to comment on any or all of the questions on the proposed standard.

We appreciate both formal and informal comments, whether supportive or critical, as both supportive and critical comments are essential for us to reach a balanced view.

Making a submission

Submissions on this consultation can be provided via any of the avenues below:

- On our 'Open for Comment' page on our [website](#)
- Emailing us: assurance@xrb.govt.nz
- Sending a letter to: External Reporting Board, PO Box 11250, Manners Street, Wellington 6142

The consultation closes on DATE

○ DATE

Open for comment

○ Consultation

Keep an eye on our website for details on events and information relating to this consultation, such as:

Walkthrough Webcast

Virtual feedback forum

○ DATE

Consultation closes

Publication of submissions, the Official Information Act and the Privacy Act

We intend to publish all submissions on our website, unless the submission may be defamatory. If you have any objection to publication of your submission, we will not publish it on the XRB website. However, it will remain subject to the Official Information Act 1982 and, therefore, it may be released in part or in full. The Privacy Act 2020 also applies.

If you have an objection to the release of any information contained in your submission, we would appreciate you identifying the parts of your submission to be withheld, and the grounds under the Official Information Act 1982 for doing so.



PART TWO: **KEY ISSUES FOR FEEDBACK**



3.

Understanding the issues

3.1 Weighing up the potential benefits and issues

We recognise that there are a number of less complex entities that are audited, either voluntarily or by legislative requirement. We are aware of capacity constraints affecting the auditing profession, and that some view the ISA for LCE as a way to increase audit efficiency and effectiveness.

While the ISA for LCE presents expected benefits, it's important to consider any drawbacks that might arise from its adoption.

Potential benefits	Potential issues
<ul style="list-style-type: none"> Quality Focus: The ISA for LCE will help auditors deliver consistent and effective high-quality audits for LCEs. The ISA for LCE requires the auditor to comply with relevant ethical requirements, including those pertaining to independence. For quality at the audit firm level, the ISA for LCE requires that the audit engagement partner be a member of a firm that applies PES 3¹ and PES 4². Proportionate and Tailored: The standard is specifically designed for the needs of audits of less complex entities, focusing on relevant requirements that are proportionate to the typical nature and circumstances of a less complex entity. Because of this tailored approach, there are strict parameters as to the types of entities that this standard can be for. This is discussed further in the next section. Aligned with ISAs: The standard contains requirements that are based on the underlying concepts from the full suite of ISAs and ISAs (NZ) but are proportionate and tailored to the specific needs of a less complex entity audit. This ensures that the audit approach remains consistent with the overall objectives of the full ISAs, and the same level of reasonable 	<ul style="list-style-type: none"> Perception of Reduced Audit Quality: The audit performed in accordance with the ISA for LCE might be perceived as a lesser quality or scaled down audit, due to not being done in line with the full ISAs. This could create the perception of a "two-tier" auditing environment, raising concerns that audits conducted under the ISA for LCE, and the assurance provided, are "less than" those performed using the full ISAs. Cost saving expectations: The use of a separate standard for LCEs might create an expectation that audits conducted under this standard will be inherently "cheaper" compared to full ISA audits. This could lead to pressure for auditors to lower fees for LCE engagements, potentially impacting the quality of the work performed. It's important to emphasize that the tailored nature of the requirements of the ISA for LCE doesn't necessarily translate into lower fees, as the level of assurance remains the same. Education, training and maintenance costs: There is an increased need for education, training and maintenance for auditors and firms that would use both the full ISAs (NZ) and the ISA (NZ) for LCE standard. There is also an increased need for education of users to mitigate

¹ Professional and Ethical Standard (PES) 3 *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

² Professional and Ethical Standard (PES) 4 *Engagement Quality Reviews*

<p>assurance, while acknowledging the reduced complexity of the engagement.</p> <ul style="list-style-type: none"> • Clear, Understandable and Concise: The standard is written with clarity and using plain language, making it easy for auditors to understand and implement. • Suited for New Zealand's economic environment: New Zealand has many entities that would meet the definition of less complex entities, and either are legally required to be audited or seek out audits voluntarily. 	<p>the risk of an expectation gap and marketplace confusion. This may cause additional costs on audit firms to implement the ISA for LCE standard.</p> <ul style="list-style-type: none"> • Complexity reassessment risk: There is a risk that an entity initially assessed as a LCE may subsequently be determined to no longer meet the qualitative characteristics of a LCE. This could necessitate a reassessment of the audit approach and potentially a significant rework of the audit file already performed under the ISA for LCE.
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Alternatives

The XRB previously explored developing an alternative product using agreed-upon procedures for charities that are not required by legislation to have an audit or a review. Under this initiative, the practitioner would agree with the charity the procedures to be performed, perform those procedures and communicate the outcome in a report to enable the user of the report to draw their own conclusions based on the information provided. The report would not offer any assurance, but simply report factual findings.

Alongside this, we also explored whether the examination regime used in the UK would be suitable in New Zealand.

The ISA for LCE project's emergence and the continued voluntary uptake of audits and reviews by charities led to XRB pausing this initiative.

Global context

It's important to note that adopting the ISA for LCE is optional for jurisdictions to adopt. i.e., New Zealand can choose not to adopt the ISA for LCE. One of the reasons that the IAASB developed this standard was to prevent the jurisdictional divergence in the audit of less complex entities, where some countries were starting to develop their own specific auditing standards over LCEs.

We are aware of some jurisdictions that have already committed to using the ISA for LCE standard (e.g., Finland, Iceland and Sweden), and are also aware of some jurisdictions that have decided not to adopt (e.g. UK, Australia and Canada). The ISA for LCE may not be a good fit for jurisdictions where the legislative thresholds for audit exemption are high; where compilation work is prevalent or where alternative auditing standards are already established. Each country will decide on their own whether the ISA for LCE suits their jurisdiction.

Maintenance of the ISA for LCE

As noted above, one of the concerns emerging regarding the adoption of the ISA for LCE is the perception of a "two-tier" audit environment. The way in which the standard is maintained globally may impact on these perceptions.

Maintenance of the ISA for LCE refers to the ongoing process of keeping the standard up-to-date, and in line with revised or new auditing standards. The IAASB has committed to a 3-year period of stability meaning that

during this initial period, there will be no major revisions to the ISA for LCE. This initial period of stability will provide auditors time to adopt and implement the standard before introducing any possible revisions.

The IAASB is yet to determine how the ISA for LCE would be maintained thereafter, i.e., will the ISA for LCE be maintained periodically; developed and consulted on at the same time as revising or consulting on a new ISA; or developed and consulted shortly after the corresponding ISAs are amended. The second option may mean there is a time lag between the changes made to the full ISAs and the ISA for LCE.

An example of this is the revised *Going Concern* standard, which is expected to be applicable from June 2026. As the ISA for LCE would still be under a period of stability, new requirements arising from the revised *Going Concern* standard would not be applicable for ISA for LCE audits until at least December 2028. This may be seen as an issue in that the requirements will be inconsistent between the ISA and ISA for LCE in respect to *Going Concern* during this period, yet the same level of reasonable assurance will be provided through an ISA or ISA for LCE audit.

We are interested in your views as to whether the timing of the maintenance of the ISA for LCE globally impacts your perceptions of the audit undertaken in accordance with the ISA for LCE standard. This may be an issue if a full ISA has substantially different requirements or principles arising from its revision, and the ISA for LCE is not updated at the same time.

If you consider that the only way in which the perception issues can be tackled is to maintain the ISA for LCE at the same time as the corresponding ISA, we also seek your views as to options for New Zealand, noting there may be global inconsistency issues if the maintenance of the NZ standard get ahead of the international standard's maintenance.

1. Do you consider that the XRB should adopt the ISA for LCE in New Zealand? Why or why not?
2. Do you consider the benefits of adopting the ISA for LCE in New Zealand outweigh the costs? Are there any other expected benefits and issues which should be considered?
3. Does the timing for the maintenance of the ISA for LCE standard impact your answer to Q1? If yes, in what way and what would you recommend the XRB does?

3.2 Applicability of the standard in New Zealand

The requirements in the ISA for LCE are designed to be proportionate to the nature and circumstances of a LCE. It does not address complex matters or circumstances. If the ISA for LCE was used to audit a complex entity, compliance with the requirements of the ISA for LCE will not be sufficient for the auditor to obtain sufficient appropriate audit evidence to support a reasonable assurance opinion, because insufficient or inappropriate consideration would be given to the complex matters or circumstances.

Part A, *Authority*, of the standard describes the limitations that will make the standard inappropriate for use. Limitations are designated into three categories:

1. **Specific Prohibitions:** Specific classes of entities for which the use of the proposed standard is prohibited. Examples include a listed entity, an entity one of whose main functions is to take deposits from the public, and an entity one of whose main functions is to provide insurance to the public.
2. **Qualitative characteristics:** that if not exhibited by an entity would ordinarily preclude the use of the ISA for

LCE in the audit of that entity. All qualitative characteristics are to be considered both individually and in combination. The list is not exhaustive nor intended to be absolute (including numerical indicators).

Some of the qualitative characteristics include:

- **Business activities, business model and industry** - The business activities, business model, or the industry in which the entity operates, do not give rise to significant pervasive business risks. There are no specific laws or regulations that govern the business activities that add complexity (for example, prudential requirements). The entity's transactions result from lines of business or revenue streams.
- **Organisational structure and size** - The structure is relatively straightforward, with few reporting lines or levels and a small key management team (for example, five individuals or less).
- **Ownership structure** - The entity's ownership structure is straightforward and there is clear transparency of ownership and control, such that all individual owners and beneficial owners are known.

The ISA for LCE can be used to perform audits of group financial statements, if eligible. The group and its entities or business units are evaluated under the same criteria as discussed above, including the same qualitative characteristics, but in the context of the group. The group structure, access to information or people and the consolidation process are also considered by the auditor in determining whether or not to use the ISA for LCE.

The use of the ISA for LCE is prohibited for group audits 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 (e.g., attending a physical inventory count or physically inspecting assets or documents).

Notwithstanding that professional judgement is applied in determining whether the ISA for LCE is appropriate to use, if there is uncertainty about whether an audit meets the criteria as set out in the *Authority* of the standard, the use of the ISA for LCE is not appropriate. (i.e. if in doubt, you are out).

3. A Quantitative threshold to further limit the applicability of the standard. The IAASB provides the ability for standard setting authorities to set a quantitative threshold over which to exclude the audits of entities to be conducted using the ISA for LCE.

Strengthening the Authority in New Zealand

There are two aspects of the Authority that we are consulting on:

- (a) Specific Prohibitions
- (b) Quantitative Thresholds

(a) Specific Prohibitions

The ISA for LCE includes specific prohibitions on its use for certain types of entities, primarily those with public interest characteristics. In New Zealand, we propose to refine the specific prohibitions beyond listed entities, deposit takers, and insurers. This refinement would introduce an additional prohibition for FMC reporting entities considered to have higher level of public accountability (FMC HLPAs) in New Zealand.

This added prohibition aims to ensure that entities with a greater public interest or higher complexity remain subject to audits conducted under the full ISAs (NZ).

We considered whether other FMC reporting entities, being those considered to have a lower level of public accountability (FMC LLPAs) could also be specifically prohibited but noted that there may be entities in this

category that are less complex and could possibly be audited under this standard. Those FMC LLPA entities that have characteristics of complexity would be scoped out of the standard through the qualitative characteristics section of the Authority.

Examples of FMC entities under the Financial Markets Conduct Act 2013 (FMC Act), or through a notice issued under the FMC Act, include:

FMC reporting entities with a “higher level of public accountability” (FMC HLPAs) include	FMC reporting entities with “lower levels of public accountability” (FMC LLPAs) include
<ul style="list-style-type: none"> (a) all issuers of equity securities or debt securities; (b) listed issuers; (c) licensed derivatives issuers; (d) recipients of money from a conduit issuer; (e) licensed managed investment schemes (MIS) (in respect of the investment fund financial statements); (f) registered banks; (g) credit unions; (h) licensed insurers; (i) building societies; and (j) any other entity designated as having a higher level of public accountability by the FMA. 	<ul style="list-style-type: none"> (a) licensed MIS managers (in respect of the manager’s own financial statements); (b) licensed providers of discretionary investment management services (DIMS); (c) licensed peer-to-peer lending service providers; (d) licensed crowd funding service providers; (e) licensed supervisors; and (f) licensed market operators (domestic).

As part of our development of Part 11 *Audit of Service Performance Information*, we considered whether or not to add qualitative characteristics or specific prohibitions to the *Authority*, in that if an entity exhibited complexity in its service performance information, it could not be audited under the ISA for LCE. We determined that such adjustment to the *Authority* to include mention of service performance information was not necessary. If an entity exhibited qualitative characteristics of complexity in its operations or finances, its service performance information reporting would likely exhibit complexity as well.

4. Do you agree that FMC reporting entities with higher levels of public accountability (FMC HLPAs) should be prohibited from being audited under the ISA (NZ) for LCE?
5. Do you agree that we **do not** specifically prohibit FMC reporting entities with Lower Levels of Public Accountability (FMC LLPAs) from being audited under the ISA (NZ) for LCE?
6. Are there any other entity types that you believe that we should specifically prohibit to ensure appropriate guardrails exist around the use of the ISA for LCE in New Zealand?

(b) Quantitative Thresholds

The IAASB provides the ability for standard setting authorities to set a quantitative threshold over which to exclude the audits of entities to be conducted using the ISA for LCE, based on key metrics of the entity (e.g., revenue, total assets) or the average number of employees during the period under audit.

For New Zealand, we have considered quantitative thresholds, such as excluding all Tier 1 financial reporting

entities, or using the definition of [large](#) from the Financial Reporting Act 2013 as a quantitative threshold.

We determined that such a threshold is not needed because:

- a quantitative threshold is not necessarily an indicator of complexity.
- there could be undue audit effort in testing the accuracy of metrics used in the calculation of qualitative thresholds before determining whether the use of ISA (NZ) for LCE is appropriate.
- the specific prohibitions and qualitative characteristics will already scope out entities which have characteristics of complexity.

However, the XRB are open to considering whether one needs to be put in place should there be a strong view from stakeholders.

7. Do you agree with the XRB's position not to have a quantitative threshold within the ISA (NZ) for LCE? If not, are there any quantitative thresholds that you believe should be included?

3.3 Audit of service performance information with the ISA (NZ) for LCE

Reporting and Auditing requirements

Many Public Benefit Entities (PBEs) in New Zealand are required to report Service Performance Information (SPI) based on the applicable financial reporting standard.

Some of these PBEs are required to have their general-purpose financial report, including the service performance information, audited.

Many of these PBEs may be less complex entities. To enable the use of the ISA for LCE in New Zealand, the XRB has explored adding a specific part to the ISA for LCE to include the necessary requirements for SPI. This is included as Part 11 *Audit of Service Performance Information* in the Exposure Draft.

Development of Part 11 Audit of Service Performance Information

We considered three options:

1. Draft a new Part 11 *Audit of Service Performance Information*. This approach ensures the standard remains standalone, in that an auditor would not use it in conjunction with other ISAs (NZ) and ensure the requirements are tailored to the needs of an audit of a LCE. It works in a similar manner Part 10 *Audits of Group Financial Statements*, in that it would only be applicable if the audit of service performance information is within the scope of the audit. This was our preferred approach.
2. Amend NZ AS 1 (Revised) to allow its use by auditors of both the full ISAs (NZ) and the ISA (NZ) for LCE. This option does not support the goal of the ISA for LCE being standalone and necessitates extensive edits to NZ AS 1 (Revised). Given the standards recent introduction and applicability to the market, such changes are undesirable.
3. Exclude service performance information audits from this standard's scope. This option was not considered viable, as it would severely restrict the applicability of the ISA (NZ) for LCE in NZ to financial statement audits only, where in fact, many less complex entities in New Zealand report service performance information.

When developing the requirements of Part 11, we based them on the key requirements found in NZ AS 1 (Revised)³, but tailored them to meet the needs of a less complex entity. We also used the drafting principles set by the IAASB. These drafting principles mean that the ISA for LCE has been drafted to be:

- Clear - meaning drafted in an easy to understand and unambiguous way.
- Understandable - avoiding unnecessary words and elements and by using plain language.
- Concise - avoiding unnecessary repetition.

Part 11 has been written to follow the flow of an audit of service performance information. To this end, we have recognised that it is important for an auditor to gain an understanding of the entity and its service performance information prior to setting materiality. So, understanding what the entity does, its vision, mission and strategy and who the users of the service performance information are, will help the auditor determine what the significant elements or aspects of service performance (i.e. those things that are important to users), and then help the auditor determine the materiality considerations relevant to the service performance information.

There are a couple of areas that have been drafted differently to NZ AS 1 (Revised):

- The auditor's responsibility for designing and implementing overall responses to assessed risks of material misstatement at the service performance information level – specific requirements have been included in paragraphs 11.8.1 to 11.8.3. While these requirements are consistent with the principles outlined in ISA (NZ) 330 paragraph 5 and ISA (NZ) 240 paragraphs 29 and 30, which the auditor applies when using NZ AS 1 (Revised), these requirements have been tailored and included in Part 11 due to the standalone nature of the ISA (NZ) for LCE, where the auditor does not refer to standards outside of the ISA (NZ) for LCE. This also builds on the requirement at paragraph 11.7.2. where the auditor is required to identify and assess the risks of material misstatement at the service performance information level (which is based on paragraph 32 of NZ AS 1 (Revised))
- Materiality requirements, and Essential Explanatory Material, at paragraph 11.6.1 has clarified requirements for the auditor to consider materiality for qualitative service performance information and determine materiality for quantitative service performance information. We have also clarified that when an auditor determines materiality for quantitative service performance information, they should also set performance materiality, if relevant in the circumstances.

The ISA for LCE includes Essential Explanatory Material (EEM) in blue boxes, to provide further guidance to the auditor. Key principles used in drafting EEM are:

- EEM further explains concepts or procedures in the requirements or why procedures are undertaken, but generally does not explain how the procedures should be implemented.
- EEM does not impose a requirement or expand any requirement.
- EEM is presented to the extent that it provides essential context for understanding a concept or a requirement. There are no examples on the application of the requirement presented in EEM.

Because of the drafting principles, the ED does not include all the application material from NZ AS 1 (Revised). The decision on what application material to include as EEM is judgemental. In some areas, such as materiality, more EEM has been incorporated to provide additional clarification, as materiality can be complex to apply. The EEM is largely derived from the application material in NZ AS 1 (Revised), with some sections, such as the use of service organisations EEM, based on EEM within the ISA (NZ) for LCE.

³ NZ AS 1 (Revised) *The Audit of Service Performance Information*

Current landscape

While some PBEs have been reporting service performance information for a while, for others this reporting, and audit thereof, is relatively new. The XRB are aware of the tensions and frustrations that are emerging between preparer and auditor in respect to this information, and we continue to work to better understand these tension points and work to find solutions across the reporting ecosystem.

While we explore these issues and work for solutions, we have developed Part 11 with reference to the existing approach in NZ AS 1 (Revised), mindful to tailor the requirements and essential explanatory material to suit the needs of an audit of a less complex entity.

We appreciate all feedback on the proposed requirements with the aim of ensuring that the benefits of proposals, exceed the costs.

8. Do you support the addition of Part 11 to the ISA (NZ) for LCE?
9. Do you consider that the requirements in Part 11 are appropriately tailored for LCEs?
10. Do you agree that appropriate EEM is included in Part 11? If not, what do you recommend?
11. Do you agree that the benefits of including Part 11 exceed their cost? If not why not, and what would you recommend?
12. Are there any other comments that you wish to raise about Part 11?

3.4 New Zealand specific amendments to the ISA for LCE

If we do adopt the ISA for LCE, the XRB proposes minor amendments to harmonise the international standards with local principles and practices reflected in the full ISAs (NZ). We believe that the amendments do not result in a standard that conflicts with, or results in lesser requirements, than the international standard.

In summary, the proposed amendments relate to the following:

- Responsibilities for the financial statements being those of governance rather than management. This adjusts requirements relating to the engagement letter, auditor's report, and written representations. (Ref: Para. NZ4.2.1, NZ8.6.7 and others)
- Adding reference to the specific NZ financial reporting frameworks and the Professional and Ethical Standards, and the NZ standard setters. (Ref: EEM under P.10., NZ4.3.4., and others)
- Timing of the going concern assessment, being 12 months from the date of the auditor's current report to be consistent with the relevant ISAs (NZ). (Ref: Para. NZ9.5.20 and NZ7.4.2)
- Requiring, when applicable, the auditor to discuss facts which become known after the financial statements have been issued within a reasonable period of time with management and, where appropriate, those charged with governance. (Ref: Para. NZ8.4.7)
- Guidance for the auditor to communicate with management if the auditor will intend to rely on a written public statement. (Ref: EEM under 8.6.3.)
- Adding guidance that comparative financial statements are not included in financial statements prepared under NZ generally accepted accounting practice. (Ref: EEM under 9.7)
- Delete reference to checks/cheques in the definition of Accounting Records – as these are no longer used in New Zealand, and they are unlikely to be applicable to less complex entities. (Ref: Appendix 1)

Each amended requirement paragraph or amended EEM in proposed ISA (NZ) for LCE is prefixed by “NZ”. Amended requirement paragraphs have “[Amended by the NZAuASB]” also added to indicate that the paragraph differs from its international equivalent.

At the back of the ISA (NZ) for LCE are the *Conforming amendments arising from the ISA (NZ) for LCE*. These are based on the IAASB conforming amendments, but amend relevant New Zealand assurance standards. Broadly, these amendments add reference to the ISA (NZ) for LCE across the suite of assurance standards in New Zealand.

13. Are there any matters pertaining to the proposed New Zealand specific amendments or the *Conforming amendments arising from the ISA (NZ) for LCE* that you wish to raise?

3.5 Application date

We propose that the standard is applicable for audit engagements for periods beginning on or after 15 December 2025. We consider that this will allow sufficient time for preparation to implement the standard. If adopted, this standard will be optional to use by auditors, and can only be used in audits of less complex entities, as defined in the Authority of ISA (NZ) for LCE.

14. Do you agree with the proposed application date of periods beginning on or after 15 December 2025? If not, why not?

3.6 Other matters

Please share any additional thoughts or comments you may have regarding New Zealand adopting ISA (NZ) for LCE.

We welcome feedback on any other aspects addressed in the exposure draft or if you consider there are matters we have missed.

15. Do you have any other comments on the proposed standard? If so, please specify.



4.

Consultation Questions

Respondents are asked to consider the following specific questions and to respond to the XRB by DATE.

Questions for respondents

1. Do you consider that the XRB should adopt the ISA for LCE in New Zealand? Why or why not?
2. Do you consider the benefits of adopting the ISA for LCE in New Zealand outweigh the costs? Are there any other expected benefits and issues which should be considered?
3. Does the timing for the maintenance of the ISA for LCE standard impact your answer to Q1. If yes, in what way and what would you recommend the XRB does?
4. Do you agree that FMC reporting entities with higher levels of public accountability (FMC HLPAs) should be prohibited from being audited under the ISA (NZ) for LCE?
5. Do you agree that we do not specifically prohibit FMC reporting entities with Lower Levels of Public Accountability (FMC LLPAs) from being audited under the ISA (NZ) for LCE?
6. Are there any other entity types that you believe that we should specifically prohibit to ensure appropriate guardrails exist around the use of the ISA for LCE in New Zealand?
7. Do you agree with the XRB's position not to have a quantitative threshold within the ISA (NZ) for LCE? If not, are there any quantitative thresholds that you believe should be included?
8. Do you support the addition of Part 11 to the ISA (NZ) for LCE?
9. Do you consider that the requirements in Part 11 are appropriately tailored for LCEs?
10. Do you agree that appropriate EEM is included in Part 11? If not, what do you recommend?
11. Do you agree that the benefits of including Part 11 exceed their cost? If not why not, and what would you recommend?
12. Are there any other comments that you wish to raise about Part 11?
13. Are there any matters pertaining to the proposed New Zealand specific amendments or the *Conforming amendments arising from the ISA (NZ) for LCE* that you wish to raise?
14. Do you agree with the proposed application date of periods beginning on or after 15 December 2025? If not, why not?
15. Do you have any other comments on the proposed standard? If so, please specify.



5.

Glossary

EEM	Essential Explanatory Material
FMC HLP	FMC reporting entities considered to have Higher Level of Public Accountability
FMC LLP	FMC reporting entities considered to have Lower Level of Public Accountability
IAASB	International Auditing and Assurance Standards Board
ISA for LCE	International Standard on Auditing for Audits of Financial Statements of Less Complex Entities – the international version of ISA (NZ) for LCE.
ISA (NZ) for LCE	International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities
ISA	International Standards on Auditing
ISA (NZ)	International Standards on Auditing (New Zealand)
NZAS	New Zealand Auditing Standards
NZAASB	New Zealand Auditing and Assurance Standards Board
Part 11	The NZ specific part added to the ISA for LCE to enable the audit of Service Performance Information.
SPI	Service Performance Information
XRB	External Reporting Board

XRB STANDARDS
NAVIGATOR



ISAs (NZ) and other standards are available on the XRB Standards Navigator
<https://standards.xrb.govt.nz/standards-navigator/>



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NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	5.1
Meeting date:	7 August 2024
Subject:	Review of Service Performance Information Submission Feedback
Date:	19 July 2024
Prepared By:	Lisa Thomas

Action Required

For Information Purposes Only

Agenda Item Objectives

1. For the Board to:
 - a. CONSIDER the feedback on the exposure draft for Review of Service Performance information (SPI) whilst cognisant of the emerging themes from the SPI workshops,
 - b. DISCUSS the impact on the development of the proposed review standard for SPI.

Background

2. The proposed review standard for SPI was exposed for a 90-day consultation period closing on 17 July 2024.
3. The consultation document focused on the key stages of a review engagement and whether the proposed requirements reflect an appropriate level of work effort for a review engagement of SPI.
4. During the consultation period we held a focus group attended by a mix of 15 preparers and assurance practitioners. Feedback heard at the focus group discussion is summarised at agenda 5.4.
5. We received 5 submissions from: 2 academics, one assurance practitioner, CAANZ/CPA Australia and the Office of the Auditor General.
6. The XRB has also recently held workshops aimed at preparers, assurance practitioners and funders on service performance information to obtain an understanding of the key issues with the reporting and assurance of service performance information. Emerging themes from these workshops is discussed at agenda item 1.1.

Matters to Consider

7. Key themes that came from the consultation feedback include:
 - a. Scope
 - b. Scalability and Proportionality
 - c. Consistency with other SPI standards
 - i. Lack of clarity regarding the term appropriate and meaningful
 - d. Use of the verb “consider”

e. Response to assessed risk

The emerging themes from the SPI workshops, discussed in agenda item 1.1, relevant to this project is discussed at agenda item 5.2.

Recommendations

8. We recommend that the Board considers the feedback obtained, and how this impacts the continued development of a review standard for service performance information.

Material Presented

Agenda item 5.1	Board Meeting Summary Paper
Agenda item 5.2	Key Themes
Agenda item 5.3 (supplementary)	Submissions
Agenda item 5.4 (supplementary)	Focus Group Feedback

Feedback

Feedback for the proposed review standard for service performance information (SPI) was generally supportive. Key areas of concern raised were potential inconsistency from the use of the verb “consider” when assessing the appropriateness and meaningfulness of SPI and how the inclusion of “other procedures” has been incorporated to respond to assessed risks.

Whilst there was general agreement that the assurance conclusion proposed is clear, some noted that the assurance reporting could be simplified further. Others acknowledged the difficulty with determining materiality, with one respondent suggesting further guidance on the concept would be useful.

In addition to receiving feedback specifically on the proposed requirements, we heard concerns from both the focus group and in the submissions of wider issues surrounding the reporting and assurance of service performance information. These concerns included understanding the term “appropriate and meaningful”, completeness of the measures due to variability in reporting and the ability to obtain appropriate evidence, and the value placed on SPI reporting. These issues are in line with some of the themes emerging from the recent workshops on SPI for preparers, funders and assurance practitioners.

Other ideas emerging from the recent wider outreach that may have an impact on the proposed review standard include amending the thresholds that mandate the assurance of SPI, increasing the use of limited assurance and/or uncoupling requirements from the assurance standards that deal with the financial statements.

Key Themes

Scope

The proposed standard is scoped for tier 3 charities, however an idea that emerged from the SPI workshops is to increase thresholds to enable review as an option for larger entities. An alternative option also suggested was to enable a review or limited assurance over service performance information more generally. If either of these options are explored, we would need to consider if the proposed standard is fit for purpose for larger entities.

The challenges of applying the assurance standards written for financial information to non-financial information was also highlighted. Some suggested uncoupling the assurance requirements relating to SPI from the financial assurance standards e.g., SPI requirements should be uncoupled from the wider ISAs and be contained within a standalone standard. The proposed review standard is currently scoped to be applied concurrently with ISRE (NZ) 2400, with areas that are particularly relevant or require a different approach to SPI included in the proposed SPI review standard. This is the same approach for the auditing standard for SPI, which is to be applied in conjunction with the full ISAs.

We will continue to consider how wider work on SPI by the XRB may impact the scope of the proposed review standard and report back to the NZAuASB at the October meeting. We welcome any comments or suggestions by the Board.

Scalability and Proportionality

The XRB is currently considering assurance requirements for less complex entities. We have considered the scalability and proportionality of the proposed review standard for SPI for these types of entities. The proposed standard is applied in conjunction with and reflects a similar work effort to the review standard for financial information ISRE (NZ) 2400. ISRE (NZ) 2400 in our view, is appropriate for less complex entities as requirements are already simplified compared to an audit engagement.

We will continue to monitor wider work on SPI for any impact it may have on the scalability and proportionality of the proposed review standard for less complex entities.

Consistency with other SPI standards

Respondents were supportive of consistency between the proposed review standard and the reporting and auditing standards for SPI. In some cases, however, respondents, acknowledged difficulties currently being experienced by both preparers and assurance practitioners with SPI.

One issue raised, based on research conducted by the respondent, is the potential use and interpretation of the term “appropriate and meaningful”. The respondent felt that determining the appropriateness and meaningfulness of performance measures is highly subjective and ambiguous, creating challenges for both the preparer and assurance practitioner. Research showed that despite observing several issues with the appropriateness and meaningfulness of performance measures, auditors were reluctant to issue qualified audit reports.

We continue to work with the accounting team to explore ways to enhance the way in which both standards can work together. We will report back to the NZAuASB at the October meeting. We welcome any comments or suggestions from the Board.

Use of the verb “consider”

To assess whether the SPI is appropriate and meaningful, the proposed review standard requires the assurance practitioner to “consider” factors rather than “evaluate” those factors as required by the auditing standard. Whilst respondents acknowledged that the use of the verb to “consider” indicates a lower work effort, concerns were raised whether it is clear what the difference in work effort would look like in practice. It was recommended to include examples to provide better clarity between the different work efforts.

One respondent raised concern that the use of “consider” may further encourage a compliance mindset towards SPI and devalue the development and reporting of “appropriate and meaningful” SPI. We have also heard broader concerns regarding the compliance approach to this reporting.

Research of tier 3 charities by a respondent, found that assurance over SPI appeared peripheral and was potentially considered less valuable than financial statement audit or review by charities and assurance practitioners.

Preliminary staff recommendation is to add application material based on the IAASB drafting principles guide that describes the difference between “consider” and “evaluate” i.e. active reflection versus

identify and analysis information to conclude. Examples may also be used to demonstrate the difference e.g. documentation, use of a matrix when evaluating.

Staff will continue to work with the accounting team on the wider issue regarding the value of SPI reporting.

Response to assessed risk

We proposed that responding to assessed risk is a key area of difference in work effort between an audit and a review, therefore required obtaining sufficient appropriate evidence from enquiry, analytical and other procedures as the assurance practitioner considers necessary. We highlighted that the inclusion of “other procedures” was due to the nature of service performance information however due to the connectivity between financial and service performance information reported in many instances enquiry and analytical review procedures may be sufficient.

We received feedback that including “other procedures” in the objective, and the wording used in requirements raised a greater expectation when “other procedures” would be required. One respondent noted that due to issues with verifying SPI, they were unclear whether using predominantly enquiry and analysis could ever obtain sufficient and appropriate evidence. Another respondent felt it was only in rare circumstances that analytical procedures could not be performed over SPI.

Preliminary staff recommendation is to remove “other procedures” from the objective and requirement but to retain in the application material to highlight that “other procedures” may be required due to the qualitative nature of some performance measures. This approach should not increase work effort expectations but still highlight the need to consider “other procedures” in some instances.

We welcome comments from the Board.

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	6.1
Meeting date:	7 August 2024
Subject:	ISO Sustainability Assurance
Date:	24 July 2024
Prepared By:	Karen Tipper

Action Required

For Information Purposes Only

Agenda Item Objectives

1. To receive an update from Graeme Drake on the proposed International Organisation for Standardisation (ISO) standard for the process of validating and verifying sustainability information.
2. Graeme is the Managing Director of GED Advisory and Chair of ISO/TC 207, the working group within ISO that is working jointly with ISO/CASCO to develop the proposed standard.

Background

3. ISO is a non-governmental international organisation that was established in 1946. Since then ISO has issued 25,472 international standards that cover various aspects of technology, manufacturing and management.
4. There are currently 172 country members representing ISO and 839 technical committees and subcommittees that develop the standards. Technical committees and subcommittees are made up of international technical experts. All are volunteers.
5. Standards New Zealand, a division of MBIE, is the ISO member for New Zealand that approves and issues ISO standards for use in New Zealand.
6. ISO is currently drafting ISO 14019, parts 1 -4. These standards will cover the requirements for the validation, and verification of sustainability information as well as the requirements for the accredited bodies.

Matters to Discuss

7. Prior to the NZAuASB's discussions on sustainability competence, Graeme will brief the Board on:
 - a. Key developments in the proposed standards
 - b. Scope of the proposed standards
 - c. Assurance levels
 - d. Proposed sustainability competency principles
 - e. Timelines and updates on discussions with the IAASB/IESBA that can be shared

Material Presented

Agenda item

Board Meeting Summary Paper

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	7.1
Meeting date:	7 August 2024
Subject:	Sustainability Competence
Date prepared:	25 July 2024
Prepared by:	Nimash Bhikha

Action Required

For Information Purposes Only

Agenda Item Objective

1. This objective of this agenda item is for the Board to:
 - **NOTE** the recent international developments relating to sustainability competence for assurance engagements for accountants and non-accountants;
 - **UNDERSTAND** the current infrastructure supporting the competence of GHG and sustainability assurance practitioners; and
 - **CONSIDER** whether additional steps are required to support competence for the mandatory assurance regime over GHG emission disclosures or more broadly.

Background

2. The Board has previously raised comments relating to competence in response to the IAASB's and IESBA's developing sustainability assurance standards. These comments highlighted the importance of competence where the breadth of competence needed may be extensive and acknowledging that experts and other practitioners will be used extensively, due to the complex and broad nature of sustainability information that may be reported. These submissions stressed the importance of understanding the underlying subject matter (that is, the condition of the relevant environmental, social, economic, or cultural context).
3. We have summarised recent international developments around sustainability competence and are reflecting upon the impact this may have for the XRB when considering the types of voluntary sustainability assurance occurring in New Zealand and mandatory GHG assurance.

Recent international developments

4. Globally there is a move to upskill professional accountants on sustainability related competencies. The International Federation of Accountants (IFAC) has recently released an Exposure Draft across the International Education Standards (IES), with proposed revisions related to sustainability competence to ensure aspiring professional accountants have more baseline knowledge of sustainability and other types of assurance beyond financial statement audits (refer to summary in

Agenda Item 7.2). The IES standards also require examination of assurance competence to receive the appropriate qualifications.

5. These requirements build on the proposals within IAASB's proposed sustainability assurance standard (ISSA 5000) and the fundamental principle of professional competence and due care within the IESBA's sustainability assurance Code of Ethics. They are designed to work together to build knowledge around sustainability competences at all levels of professional accountants.
6. The International Organization for Standardization (ISO) is developing a verification/validation standard for sustainability assurance. Within this developing standard is an appendix that includes principles for sustainability assurance competence for assurance practitioners providing these services (refer to summary in Agenda Item 7.3).
7. The competency requirements in this developing sustainability ISO follows the same wording as the existing requirements contained within the greenhouse gas related ISO standards, which include specific competencies for the verification/validation of GHG emissions. However, the requirements remain broad, so they can be relevant to a range of sustainability subject matters.
8. Across all these global developments, the developing competence proposals are focussed on the overall principles of competence across sustainability related matters. There are no detailed requirements of specific subject matter competencies in any proposed standard. It is difficult to develop specific requirements which cover the broad nature of sustainability matters.
9. While both IFAC and ISO are looking to address sustainability competence for professional accountants and non-accountants respectively, these are being addressed through different mechanisms.
 - The ISO approach is to focus on the competence of individual verifiers (engagement partners) who will be providing assurance, through overall principles and competence requirements (a tiered approach). The ISO standards are generally designed to be able to be applied on a stand-alone basis, but also to be further developed upon through individual certification programmes.
 - The IFAC education standards focus on the competencies for aspiring professional accountants who enter the profession, so that all accountants have the appropriate baseline knowledge in sustainability assurance. This is designed to supplement the IAASB/IESBA standards, which include competence requirements for the engagement partner as part of their developing sustainability assurance standards (both a top-down approach and bottom-up approach).

Other relevant international developments

10. In Australia, draft legislation has proposed requirements around the assurance of climate statements from years commencing 1 July 2030 onwards. The legislation requires entities to obtain assurance from the auditor of the financial report, which allows for the existing oversight regime that is in place for regulating the financial auditor to also be applicable to these assurance services.
11. In Europe, developments in sustainability in assurance have progressed with the requirements of the Corporate Sustainability Reporting Directive (CSRD). The EU requirements create an open legislative framework, and some EU members bodies have limited this assurance to be provided by financial auditors due to existing infrastructures for oversight by financial regulators.

Exploring the existing infrastructure to principles-based standards

12. To understand the full landscape of sustainability competence requirements, we have performed an analysis of the requirements within the relevant standards across professional accountants and non-accountants (refer to Agenda Item 7.2 and 7.3).
13. In addition, below we have summarised the supporting infrastructure in place for the financial audit and accredited practitioner industries in New Zealand. This is an important mechanism to support all principles within standards.

Infrastructure to support financial auditors and ISO accredited practitioners

14. The mature infrastructures that are in place to support financial statement auditors and ISO accredited practitioners in New Zealand include:

Financial Auditors Infrastructure	ISO Accredited Practitioners Infrastructure
<ul style="list-style-type: none"> The Chartered Accountant qualification recognised in legislation (New Zealand Institute of Chartered Accountants Act 1996) 	
<ul style="list-style-type: none"> Legislative requirements which outline the scope & level of assurance, who can provide assurance, who qualifies as a licensed auditor, and licensing /oversight regime 	<ul style="list-style-type: none"> Legislative requirements to use ISO standards or accredited programmes in certain areas
<ul style="list-style-type: none"> IAASB Quality Management standards which apply to the firm around competence for engagement teams 	<ul style="list-style-type: none"> Quality control requirements which apply to the organisation around competence for engagement teams, including within varying ISOs, accreditation manuals which periodically review quality
<ul style="list-style-type: none"> Internal firm policies which outline specific requirements and global network inspection regimes which periodically review competence and quality 	<ul style="list-style-type: none"> Internal firm policies and accreditation and certification programme/scheme manuals, where relevant, which outline specific requirements for different types of subject matters
<ul style="list-style-type: none"> IESBA Code of Ethics which requires compliance with the fundamental principle of professional competence and due care in all services 	<ul style="list-style-type: none"> Ethical behaviour principles which apply to the organisation around competence for engagement teams, including within varying ISOs
<ul style="list-style-type: none"> Engagement level auditing standards which require subject matter competence and auditing skills 	<ul style="list-style-type: none"> Engagement level performance standards which apply to the individual verifiers, such as ISO 14064-3:2019
<ul style="list-style-type: none"> IFAC Education Standards for aspiring accountants which outline minimum competencies, and education and examination requirement which must be met, to enter the profession 	<ul style="list-style-type: none"> Specific subject matter competency ISO standards, such as detailed GHG competencies for validation and verification teams within ISO 14066: 2011, or recognised national accreditations (e.g. Exemplar Global)
<ul style="list-style-type: none"> Monitoring inspection regimes for accountants who are part of membership bodies, which include file inspections for compliance with relevant standards, complaint investigation and enforcement, performed by professional bodies (CA ANZ, CPA Australia) for their members 	<ul style="list-style-type: none"> For accredited programmes, competence requirements at the assurance entity level, regular file inspections and individual witness audits, for compliance with relevant standards, and investigation of complaint and corrective action requirements, by JASANZ

	<p>and review requirements within individual ISO standards.</p> <p>Like accounting membership body inspections, JAS ANZ inspections are performed regularly across all accredited programmes, to ensure requirements are followed and deficiencies are corrected/prevented going forward.</p>
<ul style="list-style-type: none"> Monitoring inspection regimes for licensed FMC auditors, and complaint investigation and enforcement performed by the external agencies, such as the Financial Markets Authority (FMA) 	
	<ul style="list-style-type: none"> The International Accreditation Forum (IAF) recognition and review of accreditation providers, such as the Joint Accreditation System of Australia and New Zealand (JAS ANZ) and International Accreditation New Zealand (IANZ)
<ul style="list-style-type: none"> The International Organization of Securities Commissions (IOSCO) recognition and review of primary securities regulators, such as the FMA 	

Infrastructure to support sustainability assurance practitioners

- The supporting infrastructure for the oversight and regulation of sustainability assurance is being developed, in different ways and at different speeds, across the world. In many jurisdictions, the regulation of sustainability assurance is being leveraged off the existing financial auditor regulation regime and the existing infrastructure already in place (for example: Australia).
- The IAASB/IESBA does not have the mandate to cover who does sustainability assurance. They are committed to developing profession-agnostic general performance sustainability assurance standard (ISSA 5000) and sustainability assurance Code of Ethics (IESSA).
- The IESBA has also established a strategic partnership with the IAF to allow for accreditation to be measured against the developing sustainability assurance Code of Ethics, which will help ensure that accredited practitioners who use ISO standards also follow consistent ethical principles as set by the IESBA.
- As such, there may be monitoring of sustainability assurance engagements performed by members of professional accounting bodies or accredited programmes, through the existing monitoring channels for these members, where relevant, if these are used by those members.

Next steps on competence for voluntary climate and sustainability assurance in New Zealand

- When considering climate statements and sustainability reporting, assurance practitioners should have specific subject matter competence on all areas they are providing assurance over, which may be difficult to specify.

20. The proposed international assurance standards over sustainability information (developed by the IAASB/IESBA) include an “all-encompassing” fundamental principle of professional competence and due care applicable to all subject matters and requires practitioners to self-evaluate their competence for each engagement. No specific competencies on subject matters are included.
21. The proposed ISO standards over sustainability information similarly include a principles-based approach to competence. While the competency requirements follow the same proposed wording as the existing requirements contained within the greenhouse gas related ISO standards, the requirements remain broad so they can be relevant to a range of sustainability subject matters.
22. In New Zealand, there are currently no mandatory assurance requirements over disclosures within the climate statements beyond GHG emissions, and no mandatory sustainability reporting, or assurance requirements over sustainability reporting.
23. We will continue to reflect upon the sustainability competence in relation to climate statement and sustainability reporting assurance, but this is not considered a priority for the XRB at this stage, given the voluntary nature of sustainability assurance engagements.

Impact on New Zealand and current mandatory GHG assurance regime

Current GHG infrastructure in New Zealand

24. The XRB’s temporary GHG assurance standard ([NZ SAE 1](#)) was developed in the context of the range of infrastructure in existence for a broad range of practitioners. There are limited legislative requirements around who can perform the engagements, with no reference to competence and no licensing or legislative monitoring. Monitoring of GHG assurance services will occur from professional bodies or accreditation bodies, where relevant.
25. The FMA also have the functions under the Financial Markets Authority Act 2011 to monitor and conduct inquiries and investigations into any matter relating to, financial markets or the activities of financial markets participants or of other persons engaged in conduct relating to those markets. This may involve performing inquiries and investigations over GHG assurance practitioners.
26. The XRB’s standards can also be voluntarily applied by individuals who may not be part of a membership body or may not be operating as part of an accredited programme and may therefore not be subject to any monitoring. As such, there could be variability in the monitoring infrastructure, based on individuals professional accounting membership status or status within an accredited programme.
27. In February 2023, the Ministry for Business, Innovation and Employment (MBIE) consulted on the licensing and monitoring infrastructure for GHG/climate assurance. This consultation has not resulted in any changes. The lack of monitoring infrastructure around GHG assurance was a deliberate decision, as the mandatory assurance regime begins.

Possible actions by the XRB

28. Because of these international developments focussing on sustainability competence, we are reflecting on whether further actions to support the competencies for GHG assurance are necessary. Assurance over GHG emission disclosures within climate statements will be mandatory for accounting periods ending on or after October 2024.

29. NZ SAE 1 requires assurance practitioners to have sufficient competence in both assurance skills and the measurement and reporting of GHG emissions, and requires compliance with one of two existing GHG assurance engagement standards – [ISAE \(NZ\) 3410](#) or ISO 14064-3: 2019.
30. As part of the development of NZ SAE 1, the Board discussed the importance of having both subject matter competence, and assurance skills competence, and the requirements emphasises both skill sets are equally important ([NZ SAE 1 Basis for Conclusions – Paragraph BC83](#)).
31. A question is whether the XRB needs to take further actions to support the competence requirements within NZ SAE 1, to stop inappropriate self-evaluation of competence, particularly as this mandatory assurance regime is new, open to different accountant and non-accountant practitioners and not subject to any licensing or monitoring. Recent [academic research](#) has found that the quality of an entity’s climate risk disclosures is higher when the assurance practitioner has appropriate climate risk expertise.
32. The XRB could prepare additional staff guidance around competence for GHG assurance engagements (for example: how assurance practitioners can identify what subject matter expertise is required for assurance assignments, and how to assess what is needed for an assurance engagement and how this could be actioned).
33. However, this guidance may not be used by current practitioners who already have internal processes in place to evaluate competence and appoint assurance teams and internal and external experts as needed. It may be a challenge to prepare guidance which would be applicable to varying sectors that require GHG assurance, and in a manner which would also be useful to practitioners.
34. We note that Climate Reporting Entities with upcoming December 2024 year-ends have begun engaging with their GHG assurance providers already. While the XRB has had questions around who can provide this assurance, there have not been direct questions around the competence requirements or how these could be assessed by preparers and practitioners. It is not the XRB’s role to decide who can provide these services. NZ SAE 1 allows for all competent and independence practitioners and for the market to decide who to appoint, with application guidance which explain the required subject matter competence ([Para A26-A32](#)).
35. We consider the competence principles within NZ SAE 1 remain appropriate at this stage, without the need for XRB to produce further guidance. GHG assurance practitioners will identify and engage relevant specific expertise as needed for individual engagements. We understand the firms are recruiting and engaging GHG experts, where considered necessary, as part of preparing for these assurance services.

Questions for the Board

36. We would appreciate the Board’s views on whether any additional guidance by the XRB would be useful to GHG assurance practitioners, and if so, what questions this guidance could cover to aid practitioners’ evaluation of competence, without repeating the requirements and application material in place with NZ SAE 1 and the ethical and quality management standards (refer to Agenda Item 7.2 and 7.3).

Recommendations

37. We recommend the Board:

- **NOTE** the recent international developments relating to sustainability competence for assurance engagements;
- **UNDERSTAND** the current infrastructure supporting the competence of GHG and sustainability assurance practitioners; and
- **CONSIDER** whether additional steps are required to support competence requirements for the mandatory assurance regime over GHG emission disclosures and agree that no additional guidance on competence for GHG assurance is appropriate at this stage.

Material Presented

- Agenda Item 7.2 (Supplementary) – Sustainability Competence – Professional Accountants Analysis
- Agenda Item 7.3 (Supplementary) – Sustainability Competence – Non-Accountants Analysis

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	8.1
Meeting date:	7 August 2024
Subject:	Supporting GHG Assurance
Date:	25 July 2024
Prepared By:	Karen Tipper

Action Required

For Information Purposes Only

Agenda Item Objectives

1. This objective of this agenda item is for the Board to **NOTE** staff plans to implement our action in the prioritisation plan to hold workshops and issue guidance as needed on greenhouse gas assurance as we move to the start of the mandatory assurance period.

Background

2. Mandatory assurance over the GHG disclosures within the climate standards is effective for all reporting periods ending on or after 27 October 2024, the second year of reporting for climate reporting entities (CREs). The first climate statements for CREs with 31 December reporting periods were issued in April 2024 and we are expecting the first assurance reports to be issued in April 2025.
3. There is currently no monitoring or licensing regime for assurance practitioners who carry out these mandatory engagements but they must comply with the XRB assurance standard, namely NZ SAE 1, Assurance Engagements over Greenhouse Gas Emissions Disclosures.
4. We want to facilitate the success of this new regime and identify if there are areas where we can provide additional support and guidance if needed to supplement the standard. This paper expands on our plans to monitor developments, hold workshops and issue guidance as needed. We are particularly interested in the extent to which CREs are taking advantage of the first year of exemption to report the Scope 3 emissions and the impact this may have for assurance as some CREs will be measuring and obtaining assurance over them in the same period.

Matters to Consider

5. We are commencing delivery of a programme of education and awareness raising activities designed to support assurance over GHG emissions disclosures. This programme will span the next 6 months and will be targeted at three main audiences; assurance practitioners, users and preparers.
6. We have developed an engagement and communication plan and are currently developing a set of collateral for the different audiences that will include our key messages to enable us to respond appropriately. Possible areas that we are considering include:

- A video/interactive session interview. Mythbusters – reiterating certain requirements in the standard.
 - An assurance webinar for preparers with SBC
 - Update of Q & As/Fact sheets
 - Infographic (possibly animated)
 - Slides for presentations
 - Workshops/Sandbox sessions
7. We have a lot of interest for our first Sandbox session on 8 August. This is an exploratory session for assurance practitioners to discuss the practicalities of GHG emissions assurance under the XRB’s standard and to identify whether any further support is needed from us. This session will be facilitated group discussions covering the following:
- Scope 3 value chain emissions
 - i. Client and market readiness
 - ii. What challenges are being experienced?
 - iii. How have assurance methodologies been adapted
 - Communication Tools
 - i. Expectations re modified opinions
 - ii. Use of communication tools (key matters, other matters, Emphasis of matters)
 - Any other areas and is anything else needed from the XRB.

Recommendations

8. We recommend that the Board **NOTE** the plans to implement our action in the prioritisation plan to monitor developments on greenhouse gas assurance and provide **FEEDBACK** on any other actions we should cover.

Material Presented

Agenda item 8.1 Board Meeting Summary Paper

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	9.1
Meeting date:	7 August 2024
Subject:	Proposed Public Interest Entity Amendments to auditing and assurance standards
Date:	22 July 2024
Prepared By:	Sharon Walker

Action Required

For Information Purposes Only

Agenda Item Objectives

1. The objective of this agenda item is to:
 - consider feedback received on the domestic consultation of proposed amendments to the auditing and assurance standards for public interest entities; and
 - to obtain Board direction regarding next steps.

Background

International consultation

2. The International Auditing and Assurance Standards Board (IAASB) issued its [exposure draft](#) of proposed narrow scope amendments to the international auditing and assurance standards as a result of revisions to the definitions of listed entity and public interest entity in the international code of ethics in January 2024 for a 90 day consultation. Submissions closed on 8 April 2024.
3. The objectives of the IAASB are to achieve convergence to the greatest extent possible between the definitions and key concepts used in the international auditing and assurance and ethical standards, and to determine whether, and the extent to which, the applicability of the existing differential requirements should be expanded to apply to public interest entities.
4. For capital markets, the IAASB is catching up to the extant XRB position. Globally, the XRB supports:
 - Aligning the definition of public interest entity with the IESBA definition. We think it makes sense for the same term to be defined in the same way.
 - Expanding the application of the extant differential requirements to public interest entities (as defined in the global context). This includes expanding the mandatory engagement quality review to public interest entities and expanding the requirement to report key audit matters in the auditor's report to all public interest entities.
5. The IAASB is now in the process of considering comments with approval of a final standard expected in December 2024.
6. Due to the narrow scope of the international project, we undertook limited consultation on the international proposals, while exploring separately the impact of the proposals domestically.

Domestic consultation

7. The [domestic consultation document](#) was issued in March 2024 for a period of 90 days, with the consultation closing on 4 June. The domestic consultation focused on the implications of proposals on large public benefit entities.

Fig 1: What impact will the proposals have on audit engagements of NZ public interest entities?

	Engagement Quality Review	Key Audit Matters	Communication of other matters
FMC HPLA entities	No change	No change	No change
Large public sector	Required	Required	Required
Large charities	Required	Required	Required

8. The domestic consultation explored whether:
 - the definition of public interest entity should be the same for the auditing and assurance standards, quality management standards and the code of ethics.
 - each of the extant differential requirements should be expanded to public interest entities.
 - the benefits of the proposals outweigh the expected costs.
 - respondents have any other significant public interest matters to raise.
9. We held a virtual feedback forum in May, attended by 10 participants from a variety of backgrounds including academia, preparers, governance, member body and practitioners. Participants were well versed in the subject matter and offered rich discussion.
10. We also met separately with the Office of the Auditor-General, Charities Services, and with a focus group of practitioners to discuss the proposals and their impact on public benefit entities, in the New Zealand context.
11. Summaries of the various discussions are included in the supplemental papers. Refer agenda item 9.3.
12. Six written submissions were received.

What we heard

13. At the conceptual level, most stakeholders agree that the same definition of PIE should be used for the auditing standards, quality management and the code of ethics.
14. A minority of stakeholders supported the XRB’s proposal to expand the differential requirements from FMC reporting entities considered to have a higher level of public accountability to all PIEs.
15. However, the majority of stakeholders consider that expanding the application of the extant differential requirements to PIEs, given our broad definition, goes too far, and that the costs exceed the benefits.
16. Stakeholders are concerned about the increased cost to audit of the proposals, in particular, mandatory engagement quality review and reporting of key audit matters for all PIEs. They are concerned that the proposals will impose significant compliance costs on public sector and not for profit organisations without demonstrable benefits to users. Stakeholders are also concerned that

mandatory engagement quality review will exacerbate issues with auditor supply in an already pressured audit labour market.

17. The Office of the Auditor-General does not agree that the definition of PIE, as currently specified for application under Professional and Ethical Standard 1 should be applied to other professional and ethical standards or to auditing and assurance standards.
18. Under the Public Audit Act 2001, the Auditor-General has a statutory responsibility to satisfy himself that the audit fees charged to public entities are reasonable. The Auditor-General has indicated that if the Board proceeds with proposals for which he is unable to justify the costs, he will need to consider departing from the XRB's standards and issuing his own.
19. Stakeholder views and possible alternative ways of defining public interest entity are explored in the issues paper at agenda item 9.2.

Matters to Consider

20. We are seeking Board views on:
 - Whether, in light of the feedback received, the extant definition of public interest entity is fit for purpose.
 - Possible alternative ways to defining public interest entity and the benefits and disadvantages.

Next steps

21. We will continue to monitor international developments and bring recommendations to the NZAuASB informed by reflections from the agenda discussion and the outcome of the international process.

Material Presented

Agenda item 9.1	Board Meeting Summary Paper
Agenda item 9.2	Issues paper
Supplemental papers	
Agenda item 9.3	Submissions and other feedback

Subject: Public interest entity issues paper

1. Part 1 of this paper considers the significant issues raised by respondents to our domestic consultation on proposed changes to the auditing and assurance standards related to the IAASB's consultation on proposed narrow scope amendments for public interest entities:
 - (a) NZ Definition of public interest entity.
 - (b) Expanding the extant differential requirements to large public benefit entities.
2. Part 2 of the paper explores possible alternative ways of defining public interest entity and the advantages and disadvantages.
3. We are seeking Board views on:
 - The continued appropriateness of the current public interest entity definition in light of the feedback received from stakeholders.
 - Possible alternative options for next steps including alternative ways to define a public interest entity and the benefits and disadvantages.

Part 1: Significant issues raised on consultation

A. NZ Definition of Public Interest Entity

4. The definition of a public interest entity adopted in New Zealand, as defined in the Code of Ethics includes any entity that meets the Tier 1 criteria in accordance with XRB A1¹ and is not eligible to report in accordance with the accounting requirements of another tier. Accordingly, the New Zealand definition captures:
 - Entities that have public accountability; and
 - Entities that are large, as defined by XRB A2²
5. FMC reporting entities considered to have a higher level of public accountability are deemed to have public accountability. Large public sector and not-for-profit entities, for example, large charities are also captured under the New Zealand approach.
6. The XRB's objective in linking the public interest entity definition to the tier 1 criteria in XRB A1 was for understandability and simplicity (i.e., not introducing unnecessary complexity to the multi-sector, multi-tier approach). The XRB also considered it appropriate that audits or reviews of entities that can only report using tier 1 financial reporting requirements should be subject to the most rigorous and stringent independence rules.
7. Stakeholders agree that FMC reporting entities considered to have a higher level of public accountability are public interest entities.
8. Most stakeholders also agree that the same definition of public interest entity should be used for the auditing and quality management standards and the code of ethics.
9. It is the way in which public interest entity is defined in New Zealand, in particular in the public benefit entity space, that stakeholders have concerns about.

¹ External Reporting Board Standard (XRB) A1, *Application of the Accounting Standards Framework*

² External Reporting Board Standard (XRB) A2, *Meaning of Specified Statutory Size Thresholds*

10. On balance, stakeholders do not believe that the current public interest entity definition, as it relates to public benefit entities, is fit for purpose. In their view:
- The existing definition of public interest entity uses size as its sole criterion for determining public interest for public benefit entities. This is not an accurate reflection of risk for these entities. By comparison, for for-profit entities, public accountability determines public interest.
 - The reporting tiers were not set with audit in mind but have been used as a proxy for determining public interest for independence purposes, and the same proxy is now being proposed to apply to the differential requirements in auditing standards.
 - Large public sector and not-for-profit entities do not have the same investor relationship as for-profit entities, so financial condition is not always a primary driver for users of the financial statements. Public accountability for public benefit entities differs from for profit entities. Funders have more influence and can request information from charities.
 - The existing definition of public interest entity has previously only been considered within the context of the independence requirements of Professional and Ethical Standard 1³ (Code of Ethics). In explaining the need for differential requirements, the Code of Ethics states, stakeholders have heightened expectations regarding the independence of a firm performing an audit engagement for a public interest entity because of the significance of the public interest in the financial condition of the entity.
11. The Office of the Auditor General (OAG) has explicitly stated that it does not agree that the definition of public interest entity, as currently defined under the Code of Ethics should be applied to other professional and ethical standards or to auditing and assurance standards. In discussions with us, OAG staff commented that the concept of public interest entity is not relevant in the public sector. This is because, in carrying out their role, the Auditor-General works exclusively in the public interest.
12. The majority of stakeholders consider that the cost of expanding the application of the extant differential auditing requirements to public interest entities, given our broad definition, exceeds the benefits. In their view, additional compliance costs will result in higher audit fees having to be charged by the auditor to ensure the client generates a sufficient return for the auditor. This would reduce the funds available to these public benefit entities to spend on activities in the public interest. These additional costs are also of relevance in the current climate where public benefit entities are commonly experiencing declining revenues from their fundraising and donation activities combined or stretched government funding., along with the new requirements of having to comply with PBE FRS 48.
13. Stakeholders have also highlighted that using size as the sole criterion of public interest for public benefit entities is a crude measure and is not reflective of risk. The practitioner view is that expanding the application of the differential requirements in the auditing standards to public interest entities, given the existing broad definition of public interest entity in New Zealand, imposes more onerous requirements on New Zealand practitioners than the international standard, and that the cost of doing so exceeds the benefits.
14. As further explained in the following sections, stakeholders are concerned, given the current New Zealand definition of public interest entity, that the proposals create a disproportionate burden on large public sector and not-for profit entities without demonstrable benefit.

³ Professional and Ethical Standard 1, *International Code of Ethics for Assurance Practitioners (including International Independence Standards)* (New Zealand)

B. Expanding the differential requirements to public benefit entities

Background

15. Under the IESBA Code⁴, relevant local bodies play a pivotal role in establishing the local public interest entity definition.
16. The IESBA's mandatory categories of public interest entities are broadly defined and no recognition is given to any size or other factors that can be relevant in a specific jurisdiction. In this regard, the IESBA has departed from its normal practice of promulgating the precise definitional boundaries in the International Code.
17. Rather, the International Code provides for local bodies to more precisely define which entities should be included as public interest entities under the three mandatory categories (publicly listed entity, an entity one of whose main functions is to take deposits from the public, an entity one of whose main functions is to provide insurance to the public).
18. In order to fully adopt the IESBA's revised public interest entity definition, the relevant local body must not exclude any of the mandatory categories.
19. Additionally, the IESBA anticipates that local bodies will refine the public interest entity definition taking into account the local context to ensure that the right entities are scoped in as public interest entities in their jurisdictions. Examples of such other entities listed in the International Code that the local body might define as public interest entities include:
 - Pension funds.
 - Collective investment vehicles.
 - Private entities with large numbers of stakeholders (other than investors).
 - Not-for-profit organisations or governmental entities.
 - Public utilities.
20. As noted in its submission, the XRB agrees with, and supports the application of the differential requirements, to the mandatory categories of public interest entities as defined in the international standards.
21. The following sections of this paper explore stakeholder responses to the proposed application of the differential requirements to large public benefit entities in the New Zealand context.

B1: Engagement quality review

22. In New Zealand, a minority of stakeholders supported the proposal for mandatory engagement quality review⁵ considering it appropriate that all tier 1 reporting entities have the same safeguards in place, and questioning why, if engagement quality review is required for FMC reporting entities, it should not be required for large public sector and large not for profit entities that receive significant public funds. From a stakeholder perspective, engagement quality review provides an additional level of assurance.

⁴ International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants ("International Code")

⁵ Two stakeholders support the proposal, a practitioner and an academic

23. The majority of stakeholders,⁶ however, opposed expanding the application of the required engagement quality review to large public benefit entities. In their view, expanding the requirement to all public interest entities would be an unnecessary cost burden for audits of most large public sector and not for profit entities.
24. These stakeholders expressed the view that the protection needed for public benefit entities may differ from the protection needed for FMC reporting entities considered to have a higher level of public accountability. Public benefit entities are public interest entities by virtue of their size only, not because they have public accountability, which is the sole criterion for a for-profit entity to be a public interest entity.

Contribution to audit quality

25. Stakeholder views include:
 - An engagement quality reviewer contributes to improving/ensuring audit quality through their review and challenge of the audit work in areas of complexity, key risks and judgements made during the audit.
 - Public benefit entities for which an engagement quality review is not performed are generally entities with comparatively little complexity or subjectivity in their reporting. In these cases, the role of the engagement quality review provides significantly less incremental value and change or challenge to the audit than it does in a complex or subjective audit.
26. As well as requiring engagement quality review for certain types of entity (i.e., FMC reporting entities), Professional and Ethical Standard 3⁷ requires an engagement quality review where this is an appropriate response to quality risks.
27. The Auditor-General's criteria for engagement quality review also reflect public interest and risk. Of 295 public sector tier 1 reporting entities, 200 of these entities require engagement quality review based on the Auditor-General's criteria. Under the proposals, an additional 95 public sector audit engagements would be subject to engagement quality review without evidence that such review would improve audit quality.

Additional cost burden

28. Respondents indicated that performance of engagement quality review duties takes a significant amount of time by senior resources, adding significant incremental cost. Increased audit fees, with limited potential benefit (as discussed in the *contribution to audit quality* section) would be particularly problematic for large charities where cost pressures are already acute.
29. Respondents have also noted, in the current economic climate, not for profit entities are experiencing declining revenues from their fundraising and donation activities combined with the added cost of having to comply with the new requirements of PBE FRS 48 *Service Performance Reporting*. Auditing of the service performance information already adds to the cost of audit for public benefit entities.
30. The Auditor-General has a statutory responsibility to satisfy himself that the audit fees charged to public sector entities are reasonable. The Auditor-General has indicated that if the Board proceeds

⁶ Stakeholders opposed to expanding the engagement quality review included practitioners, preparer, governance, charities regulator (without demonstrable benefit), member body, OAG

⁷ Professional and Ethical Standard 3 (PES 3) *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

with proposals for which he is unable to justify the costs, he will need to consider departing from the XRB's standards and issuing his own.

31. In its explanatory memorandum to the exposure draft, the IAASB acknowledged that entities with a significant public interest in their financial condition would likely already be covered in the scope of entities subject to engagement quality reviews given the risk-based approach in determining engagements subject to an engagement quality review. Stakeholders told us that given the XRB's existing broad public interest entity definition this is not likely to be the case in New Zealand (i.e., a significant number of additional public benefit entities will be scoped in under the proposal).

Strain on resources

32. Stakeholder concerns include:
- Auditor rotation requirements can stretch constrained resources for audit firms when assigning a small number of key audit partners across a firm's audit portfolio.
 - The appointment of engagement quality reviewers to all public interest entities combined with the auditor rotation requirements for public interest entities may significantly reduce the availability of auditors to not-for-profit entities.
 - Smaller firms in the New Zealand market may not have sufficient capacity to meet the engagement quality review and auditor rotation requirements which would limit the availability of providers in the sector, thereby also reducing competition.
 - Any firm with 3 or fewer partners would be unable to audit these charities for more than one rotation, making them highly unappealing.
 - The rotation impact on larger firms would also create challenges as only a small number of partners in these firms audit charities. As such, suitable engagement quality review resources are limited. The resulting complexity and time burden will make large charity audit engagements less appealing, and firms may reconsider whether to continue servicing and/or taking on new clients in this sector.
33. One of the reasons that the IAASB did not previously extend the engagement quality review requirement beyond listed entities was due to the unintended consequence of scoping in smaller entities. The IAASB noted that in many jurisdictions public interest entities could include very small or non-complex entities (such as small charities) and performing an engagement quality review for audits of such entities would be overly burdensome.⁸

B2: Key audit matters

34. The IAASB exposure draft proposes to expand the application of key audit matters to public interest entities. Given the current New Zealand definition of public interest entity, this would expand the application of key audit matters to large public benefit entities.
35. Participants⁹ in our virtual feedback forum outreach event were, on balance, supportive of expanding key audit matters to apply to audits of all public interest entities, including large public benefit entities.

⁸ Refer Section 3G in the [IAASB ISQM 1 explanatory memorandum](#)

⁹ Five of seven respondents (1 preparer, 1 governance, 1 academic, 2 practitioners) support expanding the differential requirement to include key audit matters for public interest entities.

36. Proponents acknowledged the value of key audit matters but also acknowledged concerns of opponents about cost and potential for key audit matters to become a boilerplate, particularly for entities that are not complex. These concerns need to be balanced with the benefits of improved transparency and engagement with the entity and governance.
37. One participant expressed the view that focusing on potential key audit matters at the start of the audit, even if it doesn't lead to a key audit matter being reported, is beneficial in the audit.
38. However, from the practitioner focus group and written submissions, practitioner stakeholders (including the OAG) are not supportive of expanding the application of key audit matters to all public interest entities. Rather, these stakeholders consider that reporting of key audit matters for large public sector and not-for-profit entity audit engagements should continue to be done on voluntary basis. Writing a key audit matter requires additional consideration to ensure that it is written in plain English and that it is consistent with the financial statements. Given the public nature of the audit report, there are often additional checks required to ensure the report is appropriate for the users, as well as enhanced dialogue with those charged with governance on the key audit matters.
39. On balance, stakeholders consider key audit matters may be of limited benefit to large public benefit entities and public sector for-profit entities because:
 - Audit committees, management, the Office of the Auditor-General and Ministers are in a position to receive detailed information about the conduct of the audit through Audit Committee reporting and directly from the auditors. Key audit matters would not be a method used by management, or those in a fiduciary capacity to obtain any additional information as regards the audit process.
 - In relation to large charities, the use of financial reporting may be very limited. Many large charities are funded by organisations that have the ability to obtain the financial information they require. Public donors generally do not consider the financial statement prior to offering donations/funding.
 - Many of the entities the requirement for key audit matters would be extended to are simple entities with limited audit complexity and judgements. Key audit matters could become boilerplate thereby diminishing their value.
40. One stakeholder's view is that the requirement for public benefit entities to prepare a statement of service performance has provided a vast improvement on information disclosed for the public interest, particularly in relation to whether an entity has used funds for the purpose intended, what it has achieved with the resources available to it and whether it could have done more with those resources.

Part 2: The way forward

41. The IAASB is currently considering comments received on its exposure draft. The IAASB will discuss the feedback in detail at its September 2024 meeting, with a view to finalising the narrow scope amendments at its December 2024 meeting.
42. In its submission to the IAASB, the XRB sought clarification whether all entities identified as public interest entities under the local code of ethics are expected to be captured as public interest entities under the local assurance standards. The XRB is seeking to clarify whether a local jurisdiction might tailor the public interest entity definitions differently for independence purposes and the differential requirements in the auditing standards.

43. We will continue to monitor the IAASB project and consider the outcome for the NZ project in due course. However, given the extent of concern raised by stakeholders regarding the cost burden of the proposals to large public benefit entities with limited benefit, we have started to explore possible options for the XRB.
44. Options to explore for public benefit entities (public sector and not-for-profit entities):
- Option 1: Wait to see how the IAASB clarifies the intent. If the intent is that the same local public interest entity definition should be used:
 - Consider whether given the concerns regarding cost, this is a reason to depart from the intent globally and retain the status quo (i.e., FMC considered to have a higher level of public accountability for differential audit requirements but a broader public interest entity definition linked to Tier 1 for independence).
 - Option 2: Exclude public sector and not-for-profit entities from the local public interest entity definition i.e. align more strongly with the mandatory categories of public interest entity and not add public benefit entities, meaning that the more stringent independence requirements would not apply to large public sector or large not-for-profit entities.
 - Option 3: Determine a separate approach for public interest entities for the public sector
 - Option 4: Determine a separate approach for public interest entities for not-for-profit entities, not linked to size alone.
 - Option 5: A narrower public interest entity definition plus guidance/onus on firms for other sector approach.

Option 1

45. Under option 1, if the IAASB clarifies that the intent is for the same local definition of public interest entity, the NZAuASB would need to consider whether, given the concerns expressed regarding costs outweighing the benefits of the differential requirements for public benefit entities, we have a compelling reason to depart from the international standards. Modifications to the international standard are acceptable provided they consider the public interest, and do not conflict with or result in lesser requirements than the international standards.
46. Staff view is that option 1 could result in lesser requirements if the global intent is for the local public interest entity definition to apply equally, as the result would be that the public interest entity independence requirements would apply to more entities than the differential requirements in the auditing standards under the XRB's standards.

Option 2:

47. Under option 2, the definition of public interest entity would be revised to exclude large public benefit entities (i.e., aligning with FMC reporting entities considered to have a higher level of public accountability). Under the IESBA approach, local bodies are responsible for setting ethics standards and are expected to add categories of public interest entities for their jurisdictions. This option might be available if the XRB determines that its current criteria for determining public interest entities, i.e., linked to entities reporting under the tier 1 accounting requirements, is no longer appropriate.
48. Revising the definition in this way would retain FMC reporting entities considered to have a higher level of public accountability. It maintains the status quo for differential requirements in the auditing standards, capturing capital market entities as contemplated by the IAASB.

49. This approach could be seen as a step back in terms of auditor independence and may create the impression that public benefit entities are less important than for-profit entities.

Option 3:

50. Option 3 involves determining a separate approach for public sector entities based on criteria determined in conjunction with the Auditor-General.
51. The concept of separate requirements for public interest entities, particularly as they relate to auditor independence, is of less relevance in the public sector as the Auditor-General works exclusively in the public interest.
52. The Auditor-General sets a higher standard for achieving independence than contained in Professional and Ethical Standard 1. The Auditor-General's standard for independence applies consistently regardless of the public organisation's size and nature¹⁰.
53. An advantage of this approach is that the Auditor-General determines which public sector entities are public interest entities and therefore to which entities the differential auditing requirements would apply. This would facilitate the Auditor-General in meeting his statutory responsibility that audit fees charged to public entities are reasonable.

Option 4:

54. Option 4 involves determining a separate approach to defining public interest entities for not-for-profit entities that is not linked to size alone.
55. An advantage of this approach is that it is more reflective of entities in which there is public interest (rather than simply by size). However, establishing the criteria will likely be challenging, as different stakeholder groups may have different views about what is important. It may also result in more, rather than fewer, entities being captured as public interest entities.

Option 5:

56. Option 5 involves a narrower local definition of public interest entity coupled with exploring alternative ways to incorporate large public benefit entities for independence purposes. For example, align the public interest entity definition with FMC reporting entity considered to have a higher level of public accountability. This narrower definition would apply to the differential auditing requirements and the independence requirements. Separately, for purposes of independence, require that certain entities (e.g., large public sector and large not-for-profit entities) be treated as public interest entities, but do not add these categories to the public interest entity definition.
57. Both Singapore and Australia apply the stricter independence requirements to public sector and not-for-profit entities without directly including these entities within their public interest entity definition.
58. The Institute of Singapore Chartered Accountants (ISCA) approach requires that the audit of large charities and large institutions of public character be conducted in compliance with the same independence requirements that apply to listed entities. The ISCA definition of public interest entity includes listed entities. The ISCA approach scopes large public benefit entities into the stricter independence requirements but without defining those entities as public interest entities. Large charities and large institutions of public character are defined terms in Singapore, based on

¹⁰ Exceptions apply to the auditor rotation requirements and for very small public organisations.

quantitative thresholds. The ISCA has not yet adopted the revised IESBA definition of public interest entity.

59. In its Code of Ethics, the Accounting Professional Ethics Standards Board (APESB) in Australia has elevated the international guidance paragraph encouraging firms to determine whether to treat other entities as public interest entities to a requirement. The APESB has also issued an [Independence Guide](#) which includes examples of public interest entities that are not listed or APRA¹¹ regulated entities.¹²
60. An advantage of the APESB approach is that it requires firms to determine which other entities to treat as public interest entities, so they are scoped into the stricter independence requirements without being scoped into the differential auditing requirements. However, this approach requires firm judgement as to which entities are treated as public interest entities for independence purposes. While the nature of the business, size and number of employees are factors to consider in making the determination, the guide does not establish thresholds. This could create inconsistency in practice with similar entities audited by different firms being treated differently.
61. However, these approaches may not meet the intent of the international standards, if the IAASB and the IESBA land in a position where the intent is that the differential auditing requirements should apply to the same entities that are required to apply the public interest entity independence requirements.

We ask for Board views on:

- **The continued appropriateness of the public interest entity definition in light of the feedback received from stakeholders.**
- **Possible alternative ways to defining public interest entity and the benefits and disadvantages.**

¹¹ Australian Prudential Regulatory Authority

¹² Independence Guide, chapter 5