

# The International Standard on Auditing for Audits of Financial Statements of Less Complex Entities (ISA for LCE)

## Authority Supplemental Guidance

AUGUST 2024



This Guidance was prepared by the IAASB staff to help jurisdictions adopt and implement the ISA for LCE.

This staff-prepared publication does not amend or override the ISA for LCE, the text of which alone is authoritative. The [ISA for LCE](#) and Basis for Conclusions (explaining the IAASB's rationale for the proposals as reflected in the standard) were published in December 2023.

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## I. Purpose

1. This publication provides additional information that may be of assistance when adopting and implementing the IAASB's International Standard on Auditing for Audits of Financial Statements of Less Complex Entities ('the ISA for LCE' or 'the standard'). The guidance has been developed to further explain matters and circumstances that may be relevant in determining the appropriate use of the ISA for LCE in accordance with Part A of the standard. This guidance may be useful to:
  - (a) *Legislative or regulatory authorities or relevant local bodies with standard-setting authority* (such as regulators or oversight bodies, jurisdictional / national standard setters, professional accountancy organizations or others with authority for setting auditing standards) when determining the permitted use of the ISA for LCE in an individual jurisdiction.
  - (b) *Firms* for developing policies or procedures in relation to the use of the ISA for LCE.
  - (c) *Engagement teams or auditors* when determining whether the standard is appropriate to use for a specific audit engagement at the client acceptance or continuance phase.

See the diagram in **Appendix 1**.

2. This staff-prepared publication does not amend or override the ISA for LCE, the text of which alone is authoritative. Reading this publication is not a substitute for reading the ISA for LCE. This Supplemental Guide is not meant to be exhaustive and reference to the ISA for LCE itself should always be made.

## II. Introduction

3. The basis for the design of the ISA for LCE is a separate standalone standard for an audit of the financial statements of an LCE that:
  - (a) Is proportionate to the typical nature and circumstances of an audit of a less complex entity, as described in the Authority of the standard (Part A);
  - (b) Is able to be used effectively and efficiently in audits of entities embodying common characteristics of being less complex to be able to obtain sufficient appropriate audit evidence to support a reasonable assurance opinion.
  - (c) Utilizes principles-based requirements using a risk-based approach to an audit so that it can be applied to entities with a wide range of circumstances that embody common characteristics of being less complex.
4. Firms and engagement teams or auditors are expected to refer to Part A to determine the appropriate use of the standard. Part A also describes the role and responsibilities for legislative or regulatory authorities or relevant local bodies with standard-setting authority to support the appropriate use of the ISA for LCE.
5. This publication provides guidance on:
  - (a) The limitations for using the ISA for LCE (**Section III**);
  - (b) The Role and Responsibilities of Legislative or Regulatory Authorities or Relevant Local Bodies with Standard-Setting Authority (**Section IV**); and
  - (c) The Role of Firms and Engagement Teams or Auditors (**Section V**).

### III. Limitations for Using the ISA for LCE

6. The approach to the Authority (Part A) of the standard is described below. It is important to understand the limitations for using the standard because the requirements in the standard have been designed to be proportionate to the typical nature and circumstance of an audit of financial statements of an LCE in the private and public sectors. The standard does not address complex matters or circumstances and, therefore, if it is used for an audit outside the scope set out in Part A of the standard, the auditor will not be able to obtain sufficient appropriate audit evidence to support an audit opinion.
7. There are three components when assessing the appropriateness of the use of the standard:
  - (a) Specific classes of entities for which the use of the standard is prohibited (see paragraphs 8–24 of this Supplemental Guide); and
  - (b) Qualitative characteristics that must be considered when assessing the appropriate use of the standard. The characteristics listed describe the typical nature and circumstances of an audit of an LCE, for which the standard includes all necessary requirements (see paragraphs 25–35 of this Supplemental Guide).
  - (c) Quantitative thresholds to be determined by legislative or regulatory authorities or relevant local bodies with standard-setting authority (see paragraphs 36–37).

In determining whether the ISA for LCE can be used, components (a), (b) and (c) must be considered. Even if an entity is not of a class that is specifically prohibited as set out in (a), the entity, by its nature, must still be an LCE for the purpose of using the standard, in accordance with:

- The qualitative characteristics as explained in (b); and
- Any quantitative thresholds, as determined by the legislative or regulatory authority(ies) or relevant local body(ies) with standard-setting authority in the jurisdiction in accordance with (c).

#### Specific Prohibitions

8. Paragraph A.1. in Part A of the standard sets out the classes of entities and circumstances for which the use of the standard is specifically prohibited:
  - (a) Some classes of entities are always prohibited from the scope of the standard (see outright prohibitions in paragraph 9).
  - (b) Other identified classes of entities can be modified by legislative or regulatory authorities or relevant local bodies with standard-setting authority (see paragraphs 10–18).
  - (c) Audits of group financial statements (group audits) when any of the group's individual entities or business units are of a class of entities for which the use of the standard is specifically prohibited, or when component auditors are involved, except in limited circumstances (see paragraphs 19–24).

### *Classes of Entities for which there is an Outright Prohibition*

9. Use of the standard is always prohibited when:
  - (a) Law or regulation prohibits the use of the standard or specifies the use of auditing standards other than the ISA for LCE for the audit of the financial statements in that jurisdiction (paragraph A.1.(a)).
  - (b) The entity is a listed entity (paragraph A.1.(b)).<sup>1</sup>

### *Classes of Entities Which Are Prohibited, But Where the Prohibition Can Be Modified*

10. Part A sets out those entities exhibiting public interest characteristics for which use of the standard has been prohibited. In addition to listed entities, Part A describes other classes of entities that may typically exhibit public interest characteristics and that could embody a level of complexity in fact or appearance for which the use of the ISA for LCE is not appropriate. The prohibition for such entities is permitted to be modified by legislative or regulatory authorities or relevant local bodies with standard-setting authority (as further explained below).
11. The ISA for LCE shall not be used if an entity falls into one of the following classes (paragraph A.1.(c)):
  - (a) An entity one of whose main functions is to take deposits from the public (paragraph A.1.(c)(i));
  - (b) An entity one of whose main functions is to provide insurance to the public (paragraph A.1.(c)(ii)); or
  - (c) An entity in a class of entities where use of the ISA 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 (paragraph A.1.(c)(iii)).
12. The entities described in paragraph A.1.(c)(i) and (ii) of the standard may also be defined by local legislation. For the purpose of the ISA for LCE, they are broadly described for global application in such a way so as to avoid any terms that are more jurisdiction specific.

### *Modifying Certain Prohibited Classes of Entities*

13. Taking into account that jurisdictions may have different circumstances, legislative or regulatory authorities or relevant local bodies with standard-setting authority may modify each of the classes of entities described in paragraph A.1.(c)(i) and (ii) of the standard by permitting a specific sub-set within a class to be able to use the standard, or by using quantitative thresholds to indicate a 'cut-off point' after which the use of the standard is prohibited for entities within a class or a sub-set of a class. Such modifications can only be made at a jurisdictional level. See the text box under paragraph 44 for an example.

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<sup>1</sup> "Listed entity" is defined as an entity whose shares, stocks or debt are quoted or listed on a recognized stock exchange or are marketed under the regulations of a recognized stock exchange or other equivalent body (see International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews for Financial Statements, or Other Assurance or Related Services Engagements*).

If an entity meets the definition of a listed entity, the audit of the entity cannot be undertaken using the ISA for LCE because there are no procedures included in the standard specific to listed entities. Listed entities have been excluded because of the significance of the public interest in these entities, regardless of complexity.

14. Notwithstanding that modifications can be made to classes of entities described in paragraph A.1.(c)(i) and (ii) of the standard, an entire class of prohibited entities cannot be removed. A legislative or regulatory authority or a relevant local body with standard-setting authority may subsequently remove or amend modifications that they have made.
15. Professional judgment is used to determine the “main function” of an entity (as described in paragraph A.1.(c)(i) and (ii) of the standard) The term “one of whose main functions” is used in order to capture entities that have other main functions such as credit and lending but also to exclude those entities for which deposit-taking or insurance is not a main function. For example, if an entity sells goods or services but receives deposits for the purpose of securing the goods or service in advance of delivery of the good or service, the main function of the entity is unlikely to be taking deposits from the public. Each situation is judged on the facts and circumstances as to what the entity’s main function is deemed to be for the purpose of using the standard.

#### *Adding Classes of Prohibited Entities*

16. Modifications at the jurisdictional level can entail adding a class or classes of entities to the list of specifically prohibited entities, because there may also be other classes of entities that exhibit public interest characteristics in that jurisdiction (see paragraph A.1.(c)(iii) of the standard).
17. Other public interest characteristics that could be considered include:
  - The nature of the business or activities of the entity, such as those entities taking on financial obligations to the public as part of the entity’s primary business.
  - Entities subject to regulatory supervision designed to provide confidence that the entity will meet its financial obligations.
  - The importance of the entity to the sector in which it operates, including how easily replaceable it is in the event of financial failure.
  - Number and nature of stakeholders including investors, customers, creditors and employees.
  - The potential systemic impact on other sectors and the economy as a whole in the event of financial failure of the entity.
18. For example, charities display public interest characteristics due to their operational activities as they deliver services for the benefit of vulnerable communities. However, the funding mechanism and the communities these charitable organizations serve vary such that the impact of their financial condition on stakeholders will vary. For instance, a jurisdiction might determine that an entity that is defined as a charity under local legislation and meets a minimum gross receipts threshold should be added to the list of entities for which the use of the ISA for LCE is prohibited. However, another jurisdiction might not make the same determination for a similar charity in its jurisdictional context.

*Audits of Group Financial Statements*

19. Paragraph A.1.(d) of the standard explains that the standard shall not be used if the audit is a group audit and:
  - (a) Any of the group's individual entities or business units meet the criteria in paragraph A.1.(b) or A.1.(c); or
  - (b) 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).
20. The Essential Explanatory Material (EEM) below paragraph A.1.(d) of the standard provides further guidance on determining if an audit is a group audit. The terms *group financial statements*, *component*, and *component auditor* are defined in Appendix 1, *Glossary of Terms*, of the standard and Part 10 sets out the special considerations that apply to a group audit.
21. "Group auditor" is intended to have a consistent meaning across the IAASB's standards, including the ISA for LCE. When deciding on the appropriateness of using of the ISA for LCE for a group audit, and when using the ISA for LCE for a group audit, "group auditor" refers to the engagement partner who is responsible for the group audit and members of the engagement team other than component auditors. The group auditor is responsible for:
  - (a) Setting the scope, timing and direction of the group audit (i.e., the overall group audit strategy and group audit plan);
  - (b) Directing and supervising component auditors and reviewing their work;
  - (c) Evaluating the conclusions drawn from audit evidence obtained as the basis for forming an opinion on the group financial statements.
22. In a group audit, the group auditor determines the components at which audit work will be performed and who will perform the work at the component level. The work can be performed by the group auditor or component auditors, noting that:
  - (a) 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).
  - (b) In some circumstances, the group auditor may perform centralized 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 (refer to examples provided below).
23. Part A of the standard prohibits the use of the ISA for LCE for group audits where component auditors are involved, except in limited circumstances. The exemption for involving component auditors is related to a physical presence being needed for a specific audit procedure for the group audit. Examples of procedures where a physical presence may be required include attending a physical inventory count, physically inspecting assets or documents (e.g., bonds, precious metals, machinery, vehicles, etc.), or observing the performance of internal controls.
24. The involvement of component auditor(s) should be limited to the performance of the specific audit procedure. The group auditor is responsible for identifying, assessing and determining appropriate



responses to the assessed risks of material misstatement, including determining the nature, timing and extent of the further audit procedures. For example, the group auditor determines the purpose of the procedure (i.e., test of controls or substantive procedure), the type of procedure (e.g., inspection, observation), the period or date to which the audit evidence applies and the sample size, and communicates the instructions for the specific audit procedure to the component auditor and, if applicable, component management.






#### ***Examples of When Component Auditors are Involved in a Group Audit***

- ❖ The auditor has identified two components for the group audit. The audit involves two engagement teams, one for each component. Both engagement teams are under the direction and supervision of the engagement partner. The engagement team responsible for one of the components fulfills the responsibilities as group auditor. The other engagement team (i.e., component auditor) will perform audit work on the entire financial information of the other component under the direction, supervision and review of the group auditor. As the involvement of the component auditor is not limited to a specific audit procedure where a physical presence is needed, the ISA for LCE cannot be used to conduct the group audit.
- ❖ The auditor has identified two components for the group audit and the group auditor will perform all procedures required at both the components. Therefore, there are no component auditors involved in the group audit and the ISA for LCE can be used to conduct the group audit.
- ❖ The auditor has identified five components for the group audit and the group auditor will perform all procedures required at the component level. However, the group auditor has involved component auditors to observe the inventory counts for two of the components. As the involvement of the component auditors is limited to a specific audit procedure for the group audit where a physical presence is needed, the ISA for LCE can be used to conduct the group audit.

#### **Qualitative Characteristics**

25. The requirements in the standard have been designed to be proportionate to the typical nature and circumstances of an audit of an LCE. The standard 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, corporate governance arrangements of the entity, or policies, procedures or processes established by the entity.
26. The table below further describes and provides examples of the qualitative characteristics detailed in paragraph A.3. of the standard that describes characteristics of an LCE for the purpose of determining the appropriate use of the standard. The list in paragraph A.3 of the standard is intended to illustrate how the requirements in the standard have been designed for audits of LCEs. Therefore:
  - The list is not exhaustive nor intended to be absolute, 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 standard is appropriate or not in the circumstances. The matters described in the list are intended to be considered both individually and in combination.
27. Professional judgment is used in determining whether the entity exhibits the qualitative characteristics of a less complex entity and therefore whether the standard is appropriate to use. If there is uncertainty about whether, based on the list of qualitative characteristics of an LCE as set out in paragraph A.3. of the standard, an audit meets the criteria set out in the Authority, the use of the standard is not appropriate. Accordingly, application of the full ISAs, or other applicable auditing standards, would be appropriate.
28. Paragraph A.3 of the standard includes numerical indicators in relation to certain qualitative characteristics as illustrative examples only to further describe a typical LCE. They are not intended to be absolute. The auditor may conclude that a higher or lower number may be appropriate in the circumstances. These numerical indicators should be considered in the context of the particular qualitative characteristic, and in combination with the other qualitative characteristics.
29. In the table below, characteristics designated by “✓” represent those that are commonly associated with an LCE, and those designated with “✗” are those that are commonly not associated with an LCE. The characteristics in the table should be considered as explained in paragraph 26, and the presence of one ‘complex’ characteristic exhibited by an entity does not necessarily exclude the use of the ISA for LCE for that entity.

| <b>Business Activities, Business Model and Industry</b>   |   |
|---|---|
| <p><i>The entity’s business activities, business model or the industry in which the entity operates, do not give rise to significant pervasive business risks.</i></p> <p><i>There are no specific laws or regulations that govern the business activities that add complexity (e.g., prudential requirements).</i></p> <p><i>The entity’s transactions result from few lines of business or revenue streams.</i></p> |   |
|    | Business activities and business model are well established for the industry and products or services do not give rise to a significant pervasive risk of technological obsolescence, legal liability or reputational risk. |
|    | Operations are not subject to a higher degree of regulation or regulatory supervision.  |
|    | Straightforward or uncomplicated transactions resulting from few lines of business or products, requiring simple record-keeping and few internal controls.  |
|    | Products or services that give rise to a significant pervasive risk of technological obsolescence, legal liability or reputational risk.  |
|    | Operations that are subject to a high degree of regulation.<br>Note: For public sector entities, regulation is not always an indicator of complexity.   |

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| <b>X</b>  | The entity is subject to regulatory supervision, including where the entity's performance or financial position is measured against regulatory requirements such as prudential requirements, or regulatory ratio or exposure requirements.  |
| <b>X</b>  | The entity's products or services, operations or relationships are such that there is complexity in data collection and processing, including complicated transactions or accounting entries that may involve complex calculations. For example, complexity may arise when transaction processing has to account for different commercial terms with many different suppliers, customers or other parties, there are many interrelated commercial terms, or the processing of data involves many inter-related steps and the data is more difficult to identify, capture, access, understand or process |
| <b>Organizational Structure and Size</b>  |   |
| <i>The organizational structure is relatively straightforward, with few reporting lines or levels and a small key management team (e.g., 5 individuals or less).</i>                  |   |
| <b>✓</b>  | Few levels of management with responsibility for a broad range of controls, including that many controls may be directly applied by management.   |
| <b>✓</b>  | All of those charged with governance are involved in managing the entity (i.e., those with a governance role generally do not include an independent or outside member(s)).<br>Note: For charities or public sector entities, the presence of independent or outside members in a governance role is not always an indicator of complexity.   |
| <b>X</b>  | The organizational structure includes multiple levels and reporting lines to accommodate the entity's business activities.  |
| <b>X</b>  | A large key management team with many individuals involved in managing different areas of the entity.   |
| <b>X</b>  | Organizational structure that involves unusual entities or arrangements, off-balance sheet finance or other complex financing arrangements.   |
| <b>Ownership Structure</b>  |   |
| <i>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.</i> |   |
| <b>✓</b>  | An owner-managed entity, including a single owner-manager or when there is a concentration of ownership and management in a small number of individuals.  |
| <b>X</b>  | Complex ownership arrangements (e.g., joint ownership arrangements) or difficulty in determining the organization or individuals that have controlling or beneficial interests in the entity.   |

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| <b>X</b>  | The influence of related parties is unclear, such as when related parties operate through an extensive and complex range of relationships and structures.   |
| <b>Nature of Finance Function</b>   |   |
| <p><i>The entity has a centralized finance function, including centralized activities related to financial reporting.</i></p> <p><i>There are few employees involved in financial reporting roles (e.g., 5 individuals or less).</i></p>  |   |
| <b>✓</b>  | The entity's finance function performs the initiation, authorization, recording, processing, and reporting of transactions relevant to the preparation of financial statements in one location.   |
| <b>✓</b>  | The entity uses a service organization for processing straightforward or uncomplicated transactions (e.g., processing of payroll).  |
| <b>X</b>  | The entity's finance function is not centralized, for example, activities relating to the accounting and financial reporting functions are performed in a number of different locations.  |
| <b>X</b>  | The entity has a shared service center(s), whether as part of the entity itself or as part of the group to which the entity belongs, to centralize activities or processes relevant to the entity's financial reporting.  |
| <b>Information Technology (IT)</b>  |   |
| <p><i>The IT environment of the entity, including its IT applications and IT processes, is straightforward.</i></p> <p><i>The entity uses commercial software and does not have the ability to make any program changes other than to configure the software (e.g., the chart of accounts, reporting parameters or thresholds).</i></p> <p><i>Access to the software is generally limited to one or two designated individuals for the purpose of making the configurations.</i></p> <p><i>Few formalized general IT controls are needed in the entity's circumstances.</i></p> |   |
| <b>✓</b>  | The nature of the IT applications and the underlying IT infrastructure are simple, such as small, simple laptop or client server-based solution.  |
| <b>✓</b>  | The IT organizational structure is straightforward or uncomplicated, for example, the entity may not have dedicated IT resources but may have a person assigned in an administrator role for the purpose of granting employee access or installing vendor-provided updates. |
| <b>✓</b>  | The volume and complexity of data in digital form being process by the information system is low and the data is simple and able to be verified manually.   |

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| ✓ | Management may use system-generated reports in the processing of information but does not rely on these reports. Instead, management reconciles the reports back to the original documentation and verifies the calculations in the reports.  |
| ✗ | The IT organizational structure involves a dedicated IT department(s) that have structured processes, develop and implement program changes, manage access rights and are supported by personnel that have software development and IT environment maintenance skills. Alternatively, the entity may use internal or external service providers to manage certain aspects of, or IT processes within, its IT environment to meet its IT needs as indicated by the nature and extent of its business activities and related transactions and events. |
| ✗ | The entity has numerous IT systems and applications where information is passed from one IT system/application to another with complicated data interface.  |
| ✗ | The entity's IT environment includes highly customized or highly integrated IT applications, including financial reporting processes or IT applications that may be integrated with other applications (such as ERP systems).   |
| ✗ | There is a large volume of data, the data is based on complex legal or contractual terms or the data is stored in warehouses or housed with service providers (e.g., third-party storage).  |
| ✗ | Management relies heavily on complex system-generated reports in their controls.  |

**Application of the Financial Reporting Framework and Accounting Estimates**

*Few accounts or disclosures in the financial statements of the entity necessitate the use of significant management judgment in applying the requirements of the financial reporting framework.*

*The entity's financial statements ordinarily do not include accounting estimates that involve the use of methods, models, assumptions, or data, that are complex.*

Accounting estimates vary widely in nature and are subject to varying degrees of estimation uncertainty, which is the susceptibility to a lack of precision in measurement.

The financial statements of less complex entities ordinarily do not include accounting estimates that involve the use of methods or models, assumptions or data that are complex. Rather, the accounting estimates are often relatively straightforward and exhibit a lower degree of estimation uncertainty, complexity and subjectivity.

However, the presence of one or a small number of accounting estimates with a higher degree of complexity may not be indicative of the complexity of the entity as a whole and therefore the word "ordinarily" is used in the description of the qualitative characteristic, to indicate that the focus is not on isolated or "one-off" occurrences of such accounting estimates.

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| <p>In addition, accounting estimates with greater complexity may arise during the course of the audit due to unexpected events, conditions or transactions (i.e., when new information come to the auditor’s knowledge). By not focusing on isolated or “one-off” occurrences of such accounting estimates, there would be no need to “automatically” transition out of the standard during the engagement because of the complexity specific to the accounting estimate that arose during the course of the audit. However, the auditor would always need to consider if the entity is still an LCE and in certain scenarios the use of the standard would not be appropriate regardless of whether there is one or a small number of accounting estimates with a higher degree of complexity.</p> <p>When considering the complexity of accounting estimates in the determination of whether the standard is appropriate for use, using an auditor’s expert with regard to an accounting estimate is not automatically a proxy for complexity. The nature and circumstances (inherent characteristics) of the underlying accounting estimate are what drives the auditor’s determination of complexity, not necessarily the need for using an auditor’s expert.</p> |  |
| ✓   | <p>Estimate has a limited number of assumptions for which it is relatively straightforward to obtain sufficient audit evidence is straightforward and relevant information is obtainable. For example, an allowance for doubtful accounts based on applying estimated loss percentages (which can be supported by reference to actual loss experience) to respective accounts receivable aging categories.</p>   |
| ✓   | <p>Fair value accounting estimates that use quoted prices in active markets for identical assets or liabilities. Such inputs are readily available and observable. For example, International Financial Reporting Standards (IFRS) refer to such inputs as Level 1 inputs; these provide the most reliable evidence of fair value.</p>   |
| –   | <p>Fair value accounting estimates that use inputs other than quoted prices and that are observable for the asset or liability, either directly or indirectly (e.g., referred to as Level 2 inputs under IFRS) could involve varying levels of management judgment, estimation uncertainty and complexity. The specific circumstances, including whether characteristics such as those described in other examples below are present, would indicate whether it is appropriate for such an estimate to be associated with an LCE (✓ or X).</p> |
| X   | <p>Fair value accounting estimates that use unobservable inputs to measure the fair value of the asset or liability. For example, inputs which an entity develops using the best information available in the circumstances (including the entity’s own data) and that reflect the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk. IFRS refer to such inputs as Level 3.</p>   |
| X   | <p>The accounting estimate(s) is known to be associated with complicated transactions, or with accounting entries that involve significant subjectivity in judgments, complex calculations, or complex modelling.</p>  |

|          |   |
|----------|---|
| <b>X</b> | Financial instruments classified as complex under the applicable financial reporting frameworks that may distinguish accounting estimates based on the degree of complexity inherent in the recognition criteria, measurement basis, and related presentation and disclosure requirements. For example, the IFRS for Small and Medium Sized Entities (IFRS for SMEs) distinguishes between basic financial instruments and other more complex financial instruments and transactions. |
| <b>X</b> | The measurement basis required by the applicable financial reporting framework results in the need for a complex method that requires multiple sources of historical and forward-looking data or assumptions, with multiple interrelationships between them, or that use a long forecast period.  |
| <b>X</b> | Complexity in the model, as reflected by the degree to which there may be a need to apply probability-based valuation concepts or techniques, or simulation techniques to predict uncertain future outcomes or hypothetical behaviors.  |
| <b>X</b> | Difficulty in applying the method due to many valuation attributes with many interrelationships between them, the use of multiple data sets, data from multiple sources, multiple iterations of the calculation, or the calculation involves the application of sophisticated mathematical or statistical concepts.   |
| <b>X</b> | The data used is inherently difficult to understand. For example, the data used requires an understanding of technically complex business or legal concepts, or complex contractual terms.  |

30. For group audits, the following qualitative characteristics are to be considered in addition to those in paragraph 29:

| <b>Group Structure and Activities</b>   |  |
|---|--|
| <i>The group has few entities or business units (e.g., 5 or less).</i>  |  |
| <i>Entities or business units within the group operate in jurisdictions with similar characteristics, for example laws or regulations and business practices.</i> |  |
| <b>✓</b>  | The entity has two business units, one for manufacturing and one for delivering the products. However, management duties and oversight are performed by the same individual. |
| <b>✓</b>  | The group consists of a few legal entities that are based in jurisdictions with different languages but have otherwise similar characteristics.                              |
| <b>X</b>  | The parent company is based in Europe and its wholly owned subsidiary is based in a jurisdiction in Asia, where business practices differ.                                   |

|   |  |
|---|--|
| <b>X</b>  | The group structure includes many levels of subsidiaries, entities under common control, and non-controlling interests.  |
| <b>Access to Information or People</b>  |  |
| <i>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.</i>  |  |
| <b>✓</b>  | The group has a non-controlling interest in an entity that is accounted for under the equity method. There are no restrictions for the group auditor to obtain information from management of the entity in which the non-controlling interest is held (i.e., group management can facilitate access to component management).   |
| <b>X</b>  | Access to information or people at a component is restricted by component management, laws or regulations or other conditions, for example, war, civil unrest, or outbreaks of disease.  |
| <b>X</b>  | The group has a non-controlling interest in an entity that is accounted for under the equity method and the group auditor's access to component management is restricted (i.e., group management cannot facilitate access to component management). There is publicly available information, such as audited financial statements of the entity in which the non-controlling interest is held. |
| <b>Consolidation Process</b>  |  |
| <i>The group has a simple consolidation process. For example:</i>   |  |
| <ul style="list-style-type: none"> <li>• <i>Intercompany or other consolidation adjustments are not complex;</i></li> <li>• <i>Financial information of all entities or business units has been prepared in accordance with similar accounting policies applied to the group financial statements; and</i></li> <li>• <i>All entities or business units have the same financial reporting period-end as that used for group financial reporting.</i></li> </ul> |  |
| <b>✓</b>  | Intercompany transactions and balances can easily be identified when processing the consolidation adjustments.   |
| <b>✓</b>  | The differences between the accounting policies of the entities and business units and the group can easily be identified and harmonized.  |
| <b>X</b>  | The consolidation process requires 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.   |

31. When determining whether the ISA for LCE is appropriate to use on a recurring audit, the auditor considers whether the entity's characteristics have changed, or whether there are new indicators of



complexity that would result in a determination that the standard is not appropriate for use in the current period.

*Impact of Qualitative Characteristics on the Content of the Standard*

32. The ISA for LCE has been designed to be proportionate to the typical nature and circumstances of an audit of an LCE. Therefore, the standard does not contain requirements or essential explanatory material for matters or circumstances relating to prohibited entities, or matters that may increase, or indicate the presence of, complexity. Accordingly, the standard does not include any requirements addressing:
- (a) Matters that are typically relevant to listed entities, including requirements related to reporting on segment information or key audit matters.
  - (b) The involvement of component auditors. The standard shall not be used when the audit is a group audit and component auditors are involved except when component auditors' involvement is limited to circumstances in which a physical presence is needed for a specific audit procedure for the group audit. In these cases, little complexity is added compared to a situation in which no component auditors are involved
  - (c) The use of work of internal auditors (ISA 610 (Revised 2013)).<sup>2</sup> Internal auditors are often used in entities that display higher levels of complexity, to provide management with assurance over, or add value or improve an organization's operations related to risk management, controls, and governance processes.
33. In addition, because the standard only includes requirements that are proportionate to the intended nature and circumstances of an LCE, in some specific areas the standard contains requirements to address only less complex circumstances, such as:
- (a) *Accounting estimates*. Specific requirements in relation to the use of complex modelling, and requirements to address situations where there is higher estimation uncertainty (e.g., the accounting estimate is calculated using a highly specialized entity-developed model for which there are no observable inputs) have not been included as they are not expected to be relevant for the types of accounting estimates in a typical audit of an LCE.
  - (b) *Use of a service organization by the entity*. The standard includes requirements for certain circumstances where an entity uses a service organization for processing transactions. For example, many LCEs have payroll processed by a service organization (see paragraphs 6.3.11, 6.3.12 and 7.4.28). However, the ISA for LCE does not address situations that are deemed more complex relating to an entity using a service organization. For example, the standard does not contain requirements relating to the auditor's intended use of 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).
34. The standard also does not include requirements that accommodate jurisdictional-specific circumstances, in particular relating to law or regulation or reporting, as legislative or regulatory

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<sup>2</sup> ISA 610 (Revised 2013), *Using the Work of Internal Auditors*

authorities or relevant local bodies with standard-setting authority can include these where needed for that specific jurisdiction.

35. The ISA for LCE does not address additional responsibilities of auditors arising from local law, regulation or governmental authority, which may encompass a broader scope than an audit of financial statements in accordance with the ISA for LCE. These are addressed by legislative authorities or relevant local bodies with standard-setting authority within the relevant jurisdiction.

### **Quantitative Thresholds**

36. While complexity is not always directly relative to the size of an entity or its activities, complexity often increases when key quantitative measures increase. Therefore, the ISA for LCE (see paragraph A.4.) anticipates that legislative or regulatory authorities or relevant local bodies with standard-setting authority will determine quantitative thresholds for use of the standard in their jurisdictions. See paragraphs 45–49 for further guidance.
37. The inclusion of quantitative thresholds will help users of the standard understand its scope and assist with the consistent and appropriate use of the standard in a jurisdiction. The use of quantitative thresholds may also serve as an additional safeguard to limit the range of entities perceived to be within the scope of the standard.

## **IV. The Role and Responsibilities of Legislative or Regulatory Authorities or Relevant Local Bodies with Standard-Setting Authority**

38. 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 in individual jurisdictions (such as regulators or oversight bodies, jurisdictional / national auditing standard setters, professional accountancy organizations or others as appropriate).
39. In conjunction with the issuance of the ISA for LCE in a jurisdiction, legislative or regulatory authorities or relevant local bodies with standard-setting authority are expected to issue provisions and accompanying guidance for adoption and implementation of the standard, as appropriate. This may include a description of which audits are permitted to be conducted using the standard in accordance with Part A of the standard, taking into account, among other matters, the information in this supplement as appropriate. Legislative or regulatory authorities or relevant local bodies with standard-setting authority may also include additional information for firms and auditors arising from local law, regulation or governmental authority.
40. It is in the public interest to ensure that the use of the standard in individual jurisdictions is clarified as far as possible through local laws or regulations, or through modifying the classes of entities to which the standard cannot apply and determining quantitative thresholds.
41. As explained in Part A of the ISA for LCE, as part of the local adoption and implementation process, legislative or regulatory authorities or relevant local bodies with standard-setting authority:
  - Can modify the classes of entities set out in paragraph A.1.(c) of the standard (see paragraph A.2.).
  - Are anticipated to determine quantitative thresholds (see paragraph A.4.).

42. The reason for this role at jurisdictional level, is that it would not be practicable for the IAASB to define size thresholds or other criteria about what may constitute an audit of an LCE that would be capable of global application. Any further decisions (from what is already set out in the Authority of the ISA for LCE) about additional criteria or prohibitions are left to legislative or regulatory authorities or relevant local bodies with standard-setting authority.

### **Adding or Modifying Classes of Entities That May Exhibit Public Interest Characteristics**

43. The limitations set out in Part A of the standard explain the intended scope of the standard and are aimed at informing legislative or regulatory authorities or relevant local bodies with standard-setting authority regarding the types of entities for which the standard would be appropriate when making decisions to adopt or use the standard. The classes of entities set out in paragraph A.1.(c) of the Authority are broadly described, and no recognition is given to criteria that may be relevant to the nature and circumstances of entities and audits in an individual jurisdiction. Also see paragraphs 10–18.
44. When adding or modifying classes of entities that may exhibit public interest characteristics for the use of the ISA for LCE, legislative or regulatory authorities or relevant local bodies with standard-setting authority may refer to entities that are specified by law, regulation or professional standards when defining PIEs. Additional guidance that may be helpful to jurisdictions in understanding PIEs is available in IESBA's [Q&A, Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code](#) (March 2023).

#### *Examples of Jurisdictional Determinations*

The following are examples that a legislative or regulatory authority or relevant local body with standard-setting authority may consider when evaluating the adoption and use of the ISA for LCE in that jurisdiction:

- ❖ The local regulatory environment. For example, certain industries or entity types may be deemed complex based on regulations they are subject to in that jurisdiction and so it may be appropriate to add such entities to the list of audits of entities specifically prohibited from using the ISA for LCE (paragraph A.1.(c)(iii) of the standard).
- ❖ The nature of local entity structures or business models. The nature of local entity structures or business models determines that entities that meet certain criteria as listed in paragraph A.1.(c) of the standard are excluded from the scope of the ISA for LCE. However, certain entities within a prohibited class may be deemed to be LCEs for a particular jurisdiction. For example, an entity that provides insurance services but is otherwise non-complex (e.g., providers that have few insured customers and limited public exposure, and that otherwise exhibit the qualitative characteristics of an LCE set out in paragraph A.3 of the standard). It may therefore be appropriate to modify the description of the class of entities in paragraph A.1.(c)(ii) to allow the use of the ISA for LCE for audits of such entities based on set criteria in the jurisdiction.
- ❖ The nature of local industries and what may be deemed complex in that jurisdiction. It may be appropriate to add to the list of audits of entities prohibited from using the ISA for LCE audits of entities in certain sectors (e.g., cryptocurrency, exploratory mining) that may be deemed of higher complexity in a particular market (paragraph A.1.(c)(iii) of the standard).

## Determining Quantitative Thresholds

45. The ISA for LCE anticipates that legislative or regulatory authorities or relevant local bodies with standard-setting authority set quantitative thresholds in designating for which audits within that jurisdiction the standard can be used. 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. of the standard.
46. When determining quantitative thresholds, legislative or regulatory authorities or relevant local bodies with standard-setting authority may consider criteria that are commonly used for other purposes such as an entity's:
  - (a) Revenue.
  - (b) Net assets.
  - (c) Total assets.
  - (d) Number of employees.
47. 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.
48. Criteria that are more closely tied to the nature of the audit (e.g., number of audit hours, engagement risk profile or rating) are deemed inappropriate, as these are not consistent with the principle that the determination for use should not be driven by how the auditor chooses to perform the audit nor be determined by the auditor or firm methodology.
49. Legislative or regulatory authorities or relevant local bodies with standard-setting authority may consider existing definitions of “micro” or “small-sized” entities in their jurisdiction. While these definitions or thresholds may be used for different reasons (for example, driving the availability of grants or assistance, or for regulatory requirements), they may be appropriate examples of what may be considered “small” in a jurisdiction (also see paragraphs 36–37). The Authority includes two examples of existing definitions or thresholds in a jurisdiction, developed for different purposes, that may be used as quantitative thresholds for when the ISA for LCE is appropriate for use, when adjusted for the economic and other circumstances of a jurisdiction. The examples in the standard were derived from the European Commission’s website<sup>3</sup> and from the South African Department of Small Business Development’s website<sup>4</sup> during the finalization of the standard in September 2023. The Authority will not be further revised for subsequent changes from these sources, but any new size criteria established by those sources may be appropriate in future determinations about whether the standard can be used.

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<sup>3</sup> European Commission’s website: [https://single-market-economy.ec.europa.eu/smes/sme-definition\\_en](https://single-market-economy.ec.europa.eu/smes/sme-definition_en)

<sup>4</sup> South African Department of Small Business Development’s website:  
[https://www.gov.za/sites/default/files/gcis\\_document/201903/423041gon399.pdf](https://www.gov.za/sites/default/files/gcis_document/201903/423041gon399.pdf)

## V. The Role of Firms and Engagement Teams or Auditor

### Firms

50. Firms are responsible for establishing policies or procedures in relation to the permitted use of the ISA for LCE by their engagement teams. In doing so, a firm takes into account the specific prohibitions for use in Part A of the standard, any further modifications or prohibitions relevant to the applicable jurisdiction, the qualitative characteristic of an LCE, and any quantitative thresholds set for the firm's jurisdiction.
51. Firms may also further restrict use of the standard for audits of particular classes of entities or industries, by setting policies or procedures for the use of the ISA for LCE. For example, this may be based on quality risks that result from the nature and circumstances of such engagements performed by the firm.
52. Determinations by firms in their policies or procedures relating to the use of the standard should not conflict with or override the prohibitions within the standard, or any determinations made by legislative or regulatory authorities or relevant local bodies with standard-setting authority as to the authority of the standard in the relevant jurisdiction.

### Engagement Teams or Auditors

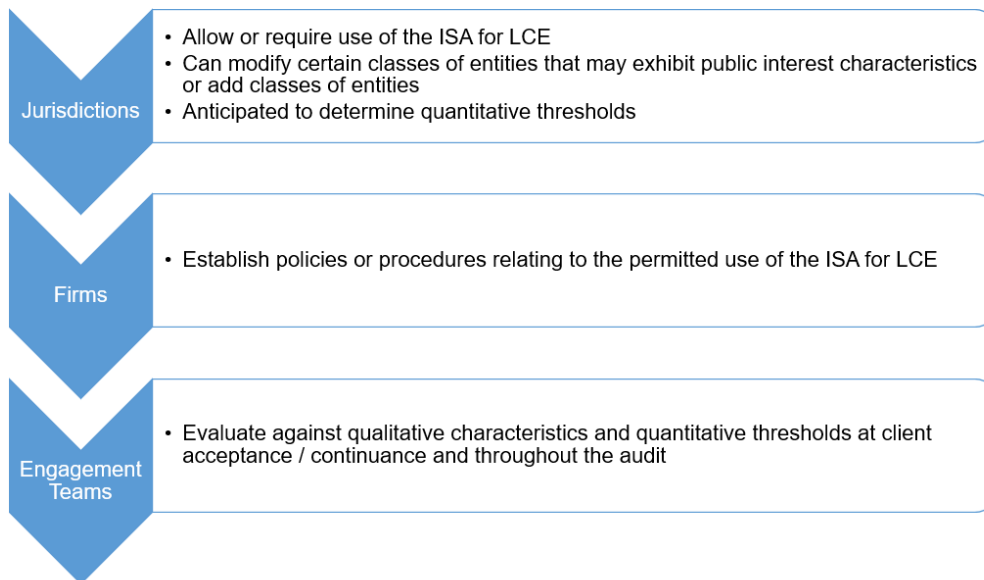
53. If a jurisdiction does not prohibit the use of the ISA for LCE, and the firm's policies or procedures allow use of the standard, the engagement partner is required to evaluate whether the use of the standard is appropriate for a particular audit engagement.
54. For individual engagements, in order to use the standard, the engagement partner is required to determine that the audit engagement is an audit of a LCE when accepting or continuing an engagement (see paragraph 4.3.1. in Part 4). This determination is based on:
  - The list of entities for which the use of the standard is specifically prohibited as set out in the local jurisdiction (see paragraphs A.1 and A.2 of the standard);
  - The qualitative characteristics of an LCE (see paragraph A.3 of the standard); and
  - Quantitative thresholds (see paragraph A.4 of the standard); and
  - The firm's related policies or procedures.

See also the diagram in **Appendix 2**.

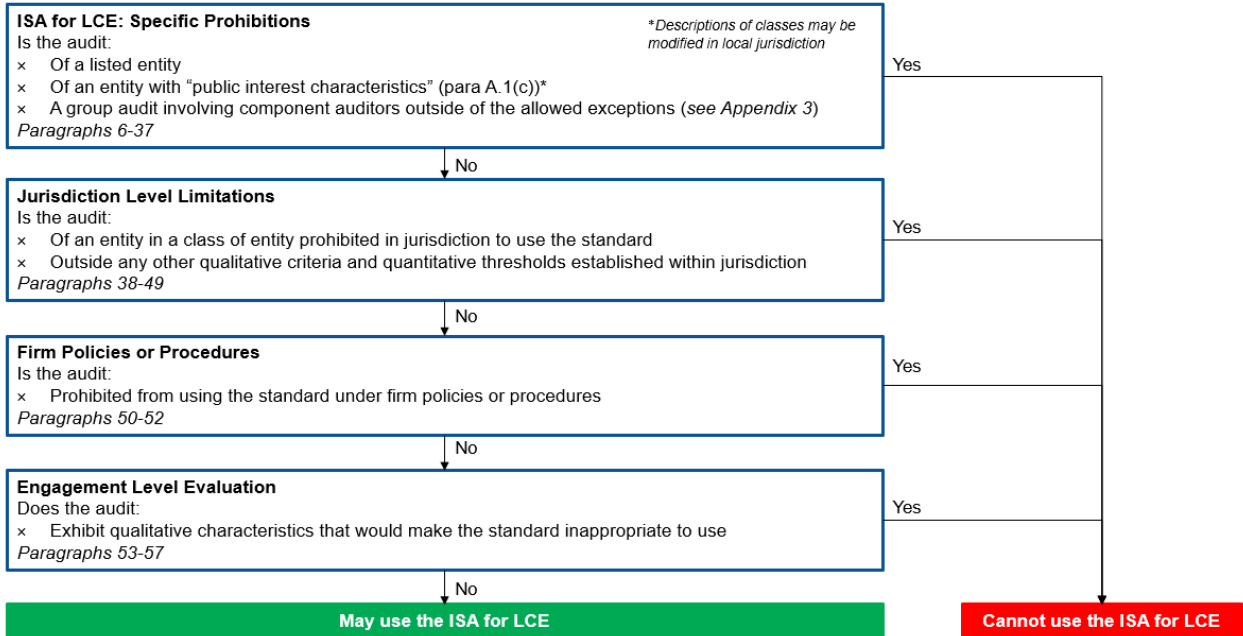
55. In undertaking procedures to obtain an understanding of the entity and its environment, the applicable financial reporting framework and the entity's system of internal control for the purpose of identifying and assessing the risks of material misstatement, new information may come to the auditor's attention that may change the engagement partner's original determination to use the standard. Accordingly, there is a 'stand-back' requirement (see paragraph 6.5.1. in Part 6) for the engagement partner to evaluate whether the ISA for LCE continues to be appropriate for the nature and circumstances of the entity being audited.
56. The standard also requires that the audit documentation includes information about any changes to the determination of the use of the ISA for LCE if further information comes to the auditor's attention during the audit that may change the professional judgment made in this regard (see paragraph 4.7.3 in Part 4).

57. If the standard is used for audit engagements other than those contemplated in its design, the auditor will not obtain sufficient appropriate audit evidence to support a reasonable assurance opinion. In such instance, the auditor also is prohibited from representing compliance with the ISA for LCE in the auditor's report. If it is found that the use of the standard is not appropriate at either the acceptance and continuance phase, or during the course of the audit (because matters of complexity not contemplated by the standard have arisen), the audit will need to be transitioned to being undertaken under the ISAs or other applicable auditing standards, as appropriate.

## Authority: Responsibilities

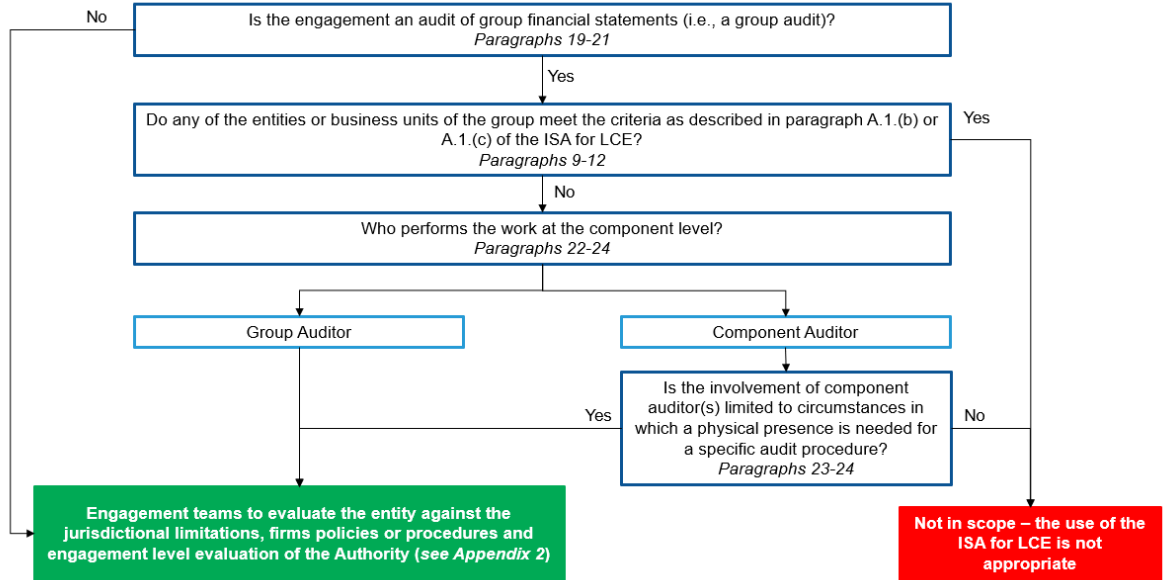


Authority: Steps to Take





Authority: Group Audit Considerations



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