

Draft IDW Auditing Standard for Less Complex Entities: Overarching Requirements for a Financial Statement Audit (IDW AuSLCE 2)

IDW AuSLCE 2

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Within the context of the audit of financial statements of small and medium-sized entities (SMEs) as a model, the Hauptfachausschuss (HFA) [Auditing and Assurance Board] issued the following draft IDW Auditing Standard for Less Complex Entities: Overarching Requirements for a Financial Statement Audit.

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1 Performance of an Audit in Accordance with IDW LCE Standards

- 1 The auditor shall comply with all Auditing Standards for LCE (AuSLCE) when performing an audit of an LCE in accordance with those standards.
- 2 The auditor shall have an understanding of the entire text of an IDW AuSLCE to understand it and to apply its requirements properly.
- 3 To achieve the overall objective of the auditor, the auditor shall:
 - (a) Determine whether any audit procedures in addition to those required by the IDW AuSLCE are necessary²; and
 - (b) Evaluate whether sufficient appropriate audit evidence has been obtained.
- 4 Subject to para. 5, the auditor shall comply with each requirement of the IDW AuSLCE unless in the circumstances of the audit the requirement is not relevant because it is conditional and the condition does not exist. The auditor need not justify why a requirement is not relevant in the circumstances unless significant professional judgment is required to determine this relevance.

¹ Issued by the HFA on December 5, 2021.

² See IDW Auditing Standard for Less Complex Entities: Scope and Preface (AuSLCE 1), para.16-18.

5 In exceptional circumstances, the auditor may judge it necessary to depart from a relevant requirement in an IDW AuSLCE. In such circumstances, the auditor shall perform alternative audit procedures to achieve the aim of that requirement.

6 If the auditor judges it necessary to depart from a relevant requirement in an IDW AuSLCE, the auditor shall document how the alternative audit procedures performed achieve the aim of that requirement, and the reasons for the departure.

The documentation requirement applies only to requirements that are relevant in the circumstances.

2 Professional Obligations

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

8 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.

9 If matters come to the engagement partner's attention that indicate that a threat to compliance with relevant ethical requirements exists, the engagement partner shall evaluate the threat through complying with the firm's policies or procedures, using relevant information from the firm, the engagement team or other sources, and take appropriate action.

10 The engagement partner shall remain alert throughout the audit engagement, through observation and making inquiries as necessary, for breaches of relevant ethical requirements or the firm's related policies or procedures by members of the engagement team.

11 If matters come to the engagement partner's attention through the firm's system of quality management, or from other sources, that indicate that relevant ethical requirements applicable to the nature and circumstances of the audit engagement have not been fulfilled, the engagement partner, in consultation with others in the firm, shall take appropriate action.

12 The auditor shall exercise professional judgement in planning and performing an audit of financial statements.

13 The auditor shall plan and perform an audit with professional skepticism recognizing that circumstances may exist that cause the financial statements to be materially misstated, whether due to fraud or error.

14 The auditor shall maintain professional skepticism throughout the audit, notwithstanding the auditor's past experience of the honesty and integrity of the entity's management and those charged with governance.

15 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.

16 If the auditor obtains new information inconsistent with the audit evidence on which the auditor originally based the identification or assessments of the risks of material misstatement, the auditor shall revise the identification or assessment³.

³ See IDW Auditing Standard for Less Complex Entities: Identification and Assessment of Risk of Material Misstatement (IDW AuSLCE 4).

- 17 Where responses to inquiries of management or those charged with governance are inconsistent, the auditor shall investigate the inconsistencies.
- 18 If the auditor has concerns about the competence, integrity, ethical values or diligence of management, or about its commitment to or enforcement of these, the auditor shall determine the effect that such concerns may have on the reliability of representations (oral or written) and audit evidence in general.
- 19 If the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter, the auditor shall document how the auditor addressed the inconsistency.
- 20 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.
- 21 During the audit, the auditor shall remain alert to the possibility that audit procedures other than those applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention.

3 Responsibilities of Engagement Partner

- 22 The engagement partner shall take overall responsibility for managing and achieving quality on the audit engagement, including taking responsibility for creating an environment for the engagement that emphasizes the firm's culture and expected behavior of engagement team members. In doing so, the engagement partner shall be sufficiently and appropriately involved throughout the audit engagement such that the engagement partner has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement.
- 23 In creating the environment described in paragraph 22, the engagement partner shall take responsibility for clear, consistent and effective actions being taken that reflect the firm's commitment to quality and establish and communicate the expected behavior of engagement team members, including emphasizing:
- (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 to the members of the engagement team;
 - (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 each engagement team member exercising professional skepticism throughout the audit engagement.
- 24 If the engagement partner assigns the design or performance of procedures, tasks or actions related to a requirement of a IDW AuSLCE to other members of the engagement team to assist the engagement partner in complying with the requirements of the IDW AuSLCEs, the engagement partner shall continue to take overall responsibility for managing and achieving quality on the audit engagement through direction and supervision of those members of the engagement team, and review of their work.
- 25 The engagement partner shall take responsibility for other members of the engagement team having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the audit engagement, and the firm's related policies or procedures, including those that address:

- (a) Identifying, evaluating and addressing threats to compliance with relevant ethical requirements, including those related to independence;
 - (b) Circumstances that may cause a breach of relevant ethical requirements, including those related to independence, and the responsibilities of members of the engagement team when they become aware of breaches; and
 - (c) The responsibilities of members of the engagement team when they become aware of an instance of non compliance with laws and regulations by the entity.
- 26** The engagement partner shall take responsibility for the direction and supervision of the members of the engagement team and the review of their work.
- 27** The engagement partner shall determine that the nature, timing and extent of direction, supervision and review is:
- (a) Planned and performed in accordance with the firm's policies or procedures, professional standards and applicable legal and regulatory requirements; and
 - (b) Responsive to the nature and circumstances of the audit engagement and the resources assigned or made available to the engagement team by the firm.
- 28** The engagement partner shall review audit documentation at appropriate points in time during the audit engagement, including audit documentation relating to:
- (a) Significant matters;
 - (b) Significant judgments, including those relating to difficult or contentious matters identified during the audit engagement, and the conclusions reached; and
 - (c) Other matters that, in the engagement partner's professional judgment, are relevant to the engagement partner's responsibilities.
- 29** The engagement partner shall take responsibility for:
- (a) Obtaining 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;
 - (b) Determining the relevance and effect on the audit engagement of the information referred to in paragraph 25(a) and take appropriate action; and
 - (c) Remaining alert throughout the audit engagement for information that may be relevant to the firm's monitoring and remediation process and communicate such information to those responsible for the process.
- 30** The engagement partner shall:
- (a) Take responsibility for the engagement team undertaking consultation on:
 - (i) Difficult or contentious matters and matters on which the firm's policies or procedures require consultation; and
 - (ii) Other matters that, in the engagement partner's professional judgment, require consultation;
 - (b) Determine that members of the engagement team have undertaken appropriate consultation during the audit engagement, both within the engagement team, and between the engagement team and others at the appropriate level within or outside the firm;
 - (c) Determine that the nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted; and
 - (d) Determine that conclusions agreed have been implemented.

- 31 The auditor shall include in the audit documentation the nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement and how such conclusions were implemented.

4 Differences of Opinion

- 32 If differences of opinion arise within the engagement team, or individuals performing activities within the firm's system of quality management, including those who provide consultation, the engagement team shall follow the firm's policies or procedures for dealing with and resolving such differences of opinion.

- 33 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) Determine that conclusions reached are documented and implemented; and
- (c) Not date the auditor's report until any differences of opinion are resolved.

5 Obtaining Sufficient Appropriate Audit Evidence

- 34 To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence 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.

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

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

- 37 If:

- (a) audit evidence obtained from one source is inconsistent with that obtained from another; or
 - (b) the auditor has doubts over the reliability of information to be used as audit evidence,
- the auditor shall determine what modifications or additions to audit procedures are necessary to resolve the matter, and shall consider the effect of the matter, if any, on other aspects of the audit.

6 Information to be used as Audit Evidence

- 38 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 obtained from an external information source.

- 39 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 audit 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.

- 40 If information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes:

- (a) Evaluate the competence, capabilities and objectivity of that expert;
- (b) Obtain an understanding of the work of that expert; and
- (c) Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.

7 General Communication Requirements

- 41 If the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.
- 42 If management refuses to remove a limitation, the auditor shall communicate the matter to those charged with governance, unless all of those charged with governance are involved in managing the entity, and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.
- 43 The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis.
- 44 The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis:
- (a) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and
 - (b) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention.
- 45 The auditor shall include in the written communication of significant deficiencies in internal control:
- (a) A description of the deficiencies and an explanation of their potential effects; and
 - (b) Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor shall explain that
 - (i) The purpose of the audit was for the auditor to express an opinion on the financial statements,
 - (ii) 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
 - (iii) 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.
- 46 Unless all of those charged with governance are involved in managing the entity, if the auditor has identified or suspects fraud involving:
- (a) management;
 - (b) employees who have significant roles in internal control; or
 - (c) others where the fraud results in a material misstatement in the financial statements,
- the auditor shall communicate these matters with those charged with governance on a timely basis. If the auditor suspects fraud involving management, the auditor shall communicate these suspicions with those charged with governance and discuss with them the nature,

timing and extent of audit procedures necessary to complete the audit. Such communications with those charged with governance are required unless the communication is prohibited by law or regulation.

- 47 The auditor shall communicate, unless prohibited by law or regulation, with those charged with governance any other matters related to fraud that are, in the auditor's judgment, relevant to their responsibilities.
- 48 Unless all of those charged with governance are involved in managing the entity, the auditor shall communicate with those charged with governance significant matters arising during the audit in connection with the entity's related parties.
- 49 Unless all of those charged with governance are involved in management of the entity, and therefore are aware of matters involving identified or suspected non-compliance already communicated by the auditor, the auditor shall communicate, unless prohibited by law or regulation, with those charged with governance matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit, other than when the matters are clearly inconsequential.
- 50 If, in the auditor's judgment, the non-compliance referred to in paragraph 49 is believed to be intentional and material, the auditor shall communicate the matter with those charged with governance as soon as practicable.
- 51 If the auditor suspects that management or those charged with governance are involved in non-compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.
- 52 The engagement partner shall review, prior to their issuance in accordance with IDW AuSLCE 7, formal written communications to management, those charged with governance or regulatory authorities.

8 Reporting to an Appropriate Authority Outside the Entity

- 53 If the auditor has identified or suspects a fraud or non-compliance with laws and regulations, 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.

9 General Audit Documentation Requirements

- 54 The auditor shall prepare audit documentation on a timely basis.
- 55 The auditor shall prepare audit documentation 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 to comply with the IDW AuSLCEs and applicable legal and regulatory requirements;
 - (b) The results of the audit procedures performed, and the audit evidence obtained; and
 - (c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

The auditor need not include in audit documentation superseded drafts of working papers and financial statements, notes that reflect incomplete or preliminary thinking, previous copies of documents corrected for typographical or other errors, and duplicates of documents.

It is neither necessary nor practicable for the auditor to document every matter considered, or professional judgement made, in an audit. 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.

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 the team (for example, there will be no matters to document relating to team discussions or supervision). Nevertheless, the engagement partner complies with the overriding requirement in paragraph 55 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.

56 In documenting the nature, timing and extent of audit procedures performed, the auditor shall record:

- (a) The identifying characteristics of the specific items or matters tested;
- (b) Who performed the audit work and the date such work was completed; and
- (c) Who reviewed the audit work performed and the date and extent of such review.

The auditor need not document why a requirement is not relevant in the circumstances unless significant professional judgment is required to determine this lack of relevance.

The requirement to document who reviewed the audit work performed does not imply a need for each specific working paper to include evidence of review. The requirement, however, means documenting what audit work was reviewed, who reviewed such work, and when it was reviewed.

57 The auditor shall include in the audit documentation matters identified, relevant discussions with personnel, and conclusions reached with respect to fulfillment of responsibilities relating to relevant ethical requirements, including those related to independence.

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

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

60 Where matters required by the IDW AuSLCE to be communicated are communicated orally, the auditor shall include them in the audit documentation, and when and to whom they were communicated. Where matters have been communicated in writing, the auditor shall retain a copy of the communication as part of the audit documentation.