

Agenda Item

3-D

Proposed Revisions to the International Standard on Auditing for Audits of Financial Statements of Less Complex Entities

This agenda item includes changes to **Agenda Item 3-B**, shown in track changes and highlighted in yellow, resulting from comments received during the plenary session on June 16, 2026, and comments received offline.

Changes presented at the IAASB meetings in December 2025 and March 2026 are hardcoded and changes presented during the plenary on June 16, 2026 are in track changes.

6. Risk Identification and Assessment

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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~~

(aA) Determining whether events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern; and

- (b) The design of further audit procedures.

The auditor uses professional judgment 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.

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. Because of its characteristicssize, an LCE may be able to respond quickly to capitalizeexploit on opportunities but may lack reserves to sustain operations.

The identification of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, is before consideration of any related mitigating factors included in management's plans for future actions.

Some events or conditions may not cast significant doubt when considered individually, however when considered collectively with other events or conditions they may ~~do so~~ cast significant doubt on the entity's ability to continue as a going concern.

Appendix 4A sets out ~~examples of~~ events or conditions that may cast significant doubt on the entity's ability to continue as a going concern ~~relevant to less complex entities~~. [Moved from under paragraph 6.2.4]

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6.2.4. In designing and performing procedures to identify and assess risks of material misstatement, whether due to fraud or error, the auditor shall ~~consider possible risks of material misstatement arising from:~~ *consider possible risks of material misstatement arising from:*

(a) ~~Consider the presence of~~ *Fraud risk factors or error;* ~~and~~

(b) ~~Consider rRelatedRelated~~ *party relationships and transactions;* ~~and~~

(c) ~~Determine whether eEventsEvents or conditions have been identified 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.

Fraud ~~R~~risk ~~F~~factors

~~Fraud risk factors are events or conditions that indicate an incentive or pressure to commit fraud, or provide an opportunity to commit fraud, or an attitude or rationalization that justifies the fraudulent action.~~ While fraud risk factors may not necessarily indicate the existence of fraud, they have often been present in circumstances where frauds have occurred and therefore may indicate risks of material misstatement due to fraud.

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.

[Moved to under paragraph 6.2.1]

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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, journal entries and other adjustments 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~~

(cA) For going concern, how disclosures related to the entity's ability to continue as a going concern are addressed-; and

- (d) The entity's resources, including the IT environment, relevant to (a) to (cA) 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.*

Fraudulent financial reporting often involves management override of controls that otherwise may appear to be operating effectively, which may include, in relation to the entity's process to prepare its financial statements, taking advantage of inadequate information processing controls in information technology applications.

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

- *Inquiries 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.

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