

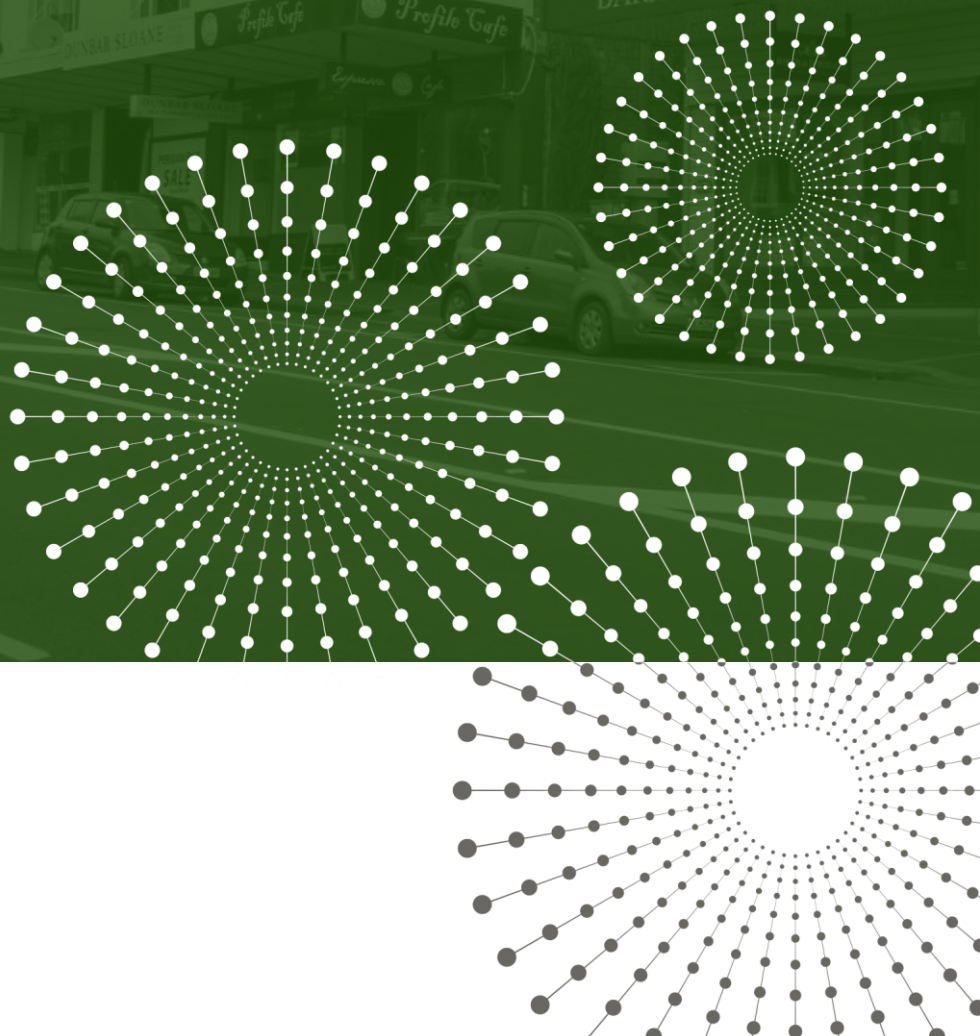
# International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities

ISA (NZ) for LCE

Explanation for decisions made



June 2025



This document relates to, but does not form part of, the ISA (NZ) for LCE, which was approved in June 2025.

It summarises the major issues raised by respondents to the Exposure Draft of the ISA (NZ) for LCE and how the NZAuASB has addressed them.

Reference should also be made to the IAASB's *Basis for Conclusions on the ISA for LCE*.

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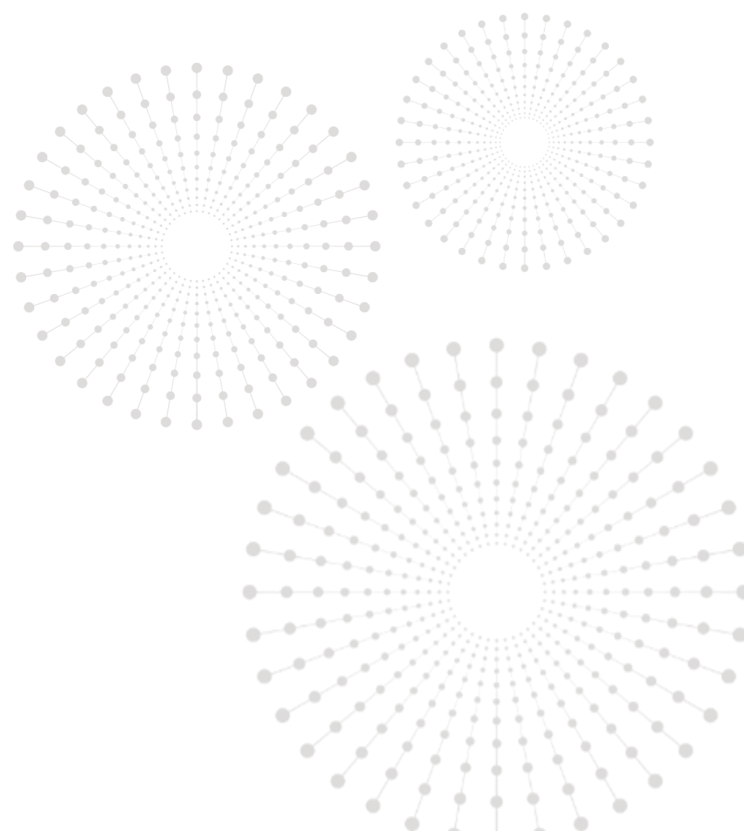
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ISBN 978-1-99-100568-7



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## Introduction

1. The *International Standard on Auditing (New Zealand) for Audits of Financial Statements of Less Complex Entities* (ISA (NZ) for LCE) is a stand-alone auditing standard available for auditors to use when auditing less complex entities. For the purposes of the standard, references to “financial statements” include “service performance information” and “entity information” where relevant.
2. The ISA (NZ) for LCE includes all relevant requirements to achieve the same level of reasonable assurance as the full suite of International Standards on Auditing (New Zealand) (ISAs (NZ)), proportionate and tailored to the nature and circumstances of a less complex entity. While it is a simpler standard, it does not result in a lesser work effort.
3. The ISA (NZ) for LCE is only available for auditors to use, if the entity meets the specific criteria of a less complex entity set out in Part A of the standard. When an audit engagement is undertaken using this standard, the ISAs (NZ) and New Zealand Auditing Standards do not apply to the engagement.

## Background

4. There had been growing concern about the length, scalability, and understandability of the International Standards on Auditing (ISAs), and their application to audits of Less Complex Entities (LCEs). In response, the IAASB developed the ISA for LCE.
5. At several points during the IAASB’s development process, the XRB engaged with stakeholders to consider whether or not to adopt this standard. In particular, in a survey of auditors and other stakeholders, conducted in August 2023, we heard that there was support for the adoption of the standard in New Zealand and for the XRB to develop requirements in a separate Part to the standard to enable the audit of service performance information of LCEs in New Zealand.
6. The IAASB issued the ISA for LCE in December 2023. Subsequently, the XRB issued a consultation document and an exposure draft, and sought feedback between November 2024-February 2025. We consulted on the following areas:
  - a. Should we adopt the standard in NZ, and if so, who would actually use the standard
  - b. Which audits should the standard apply to (the applicability)
  - c. The addition of Part 11, audit of service performance information
  - d. NZ specific amendments to the ISAs (NZ) and conforming amendments arising from the ISA (NZ) for LCE.
7. We also consulted on the benefits and costs of adoption of the standard in New Zealand. In summary, the key benefits of adopting the ISA (NZ) for LCE include:
  - **Suited for New Zealand’s environment:** New Zealand has many LCEs that are either required to have their financial statements audited or seek out audits voluntarily.
  - **Proportionate:** We are aware of capacity constraints affecting the audit profession. Some view the ISAs as increasingly long and complex, geared to large, regulated entities, making them challenging to apply. There is anxiety around compliance with very lengthy standards, in case something was missed.
  - **Tailored:** The ISA (NZ) for LCE 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. The ISA (NZ) for LCE emphasises performing the right work in the right areas.

- **Clear, Understandable and Concise:** The standard uses plain language and follows the flow of the audit, which may make it easy for auditors to understand and implement. Ease of access may enhance auditors' ability to understand and apply requirements consistently, and reduces anxiety over compliance.
- **Enhances Auditor Training:** The ISA (NZ) for LCE may be useful for training auditors, providing a clear and concise standard that is easier to understand and implement.

8. Costs or risks associated with the adoption of the standard include:

- **Perception of Reduced Audit Quality:** An audit performed in accordance with the ISA (NZ) for LCE may be perceived as a lesser quality or scaled down audit, creating the perception of a "two-tier" auditing environment. However, the ISA (NZ) for LCE does not reduce audit quality but is tailored to suit the characteristics of an LCE.
- **Costs of maintaining two suites of auditing standards:** The XRB would need to maintain two suites of auditing standards going forward. The ISA (NZ) for LCE is to be maintained and updated internationally, reducing standard setting costs.
- **Timing of the maintenance:** the ongoing maintenance of the ISA for LCE by the IAASB will create a one-year time lag between updates to the ISAs and the ISA for LCE. The IAASB is committed to maintaining consistency with the full ISAs but considered this to be the most pragmatic way to maintain the standard. The majority of respondents to our consultation did not consider the timing of maintenance to impact their view on adoption of the ISA (NZ) for LCE in New Zealand.
- **Specialisation risk:** There are questions about the long-term implications for auditors who exclusively perform audits using the ISA (NZ) for LCE and may miss opportunities to audit more complex entities. However, the market already has specialisation, and the ISA for LCE is better tailored to be applied by those who specialise in audits of LCEs in New Zealand.
- **Education and training costs:** There may be increased costs for auditors and firms that use both the ISAs (NZ) and the ISA (NZ) for LCE. There is an increased need for education of users to mitigate the perception risks. There may also be costs of training new auditors entering the profession to use this standard. There will be an increased need for the XRB to promote adoption and facilitate implementation.
- **Audit fee pressures:** There may be an expectation that audits conducted under the ISA (NZ) for LCE will be "cheaper". This could lead to pressure for auditors to lower fees, potentially impacting the quality of the work. It is important to emphasise that the tailored nature of the requirements of the ISA (NZ) for LCE doesn't necessarily translate into lower fees, as the level of assurance remains the same.
- **Complexity assessment risk:** There may be a risk that an entity initially assessed as less complex may subsequently be determined to no longer meet the qualitative characteristics of a LCE. This would necessitate use of the full ISAs and potentially a significant rework of the audit file in that year. Early adopters experience is that this is not the case. The IAASB has issued guidance to assist in a transition to the full ISAs mid-engagement if it were to occur.

9. Based on feedback received our New Zealand stakeholders agree that the costs and risks will be offset by the benefits of having an auditing standard tailored for the audit of a less complex entity. Our feedback confirms that a number of auditors would use this standard, if made available for use.

## What we heard

10. The XRB received 26 written submissions and obtained additional feedback from virtual events held during the consultation process of the exposure draft. Overall, respondents were supportive of the adoption of the standard.

### Applicability

11. The ISA (NZ) for LCE is designed to be proportionate to the nature and circumstances of a LCE. It does not address complex circumstances. Compliance with the requirements of the ISA (NZ) for LCE would not be sufficient to obtain sufficient appropriate audit evidence to support a reasonable assurance opinion for a complex entity, because insufficient or inappropriate consideration would be given to the complex matters or circumstances.
12. Part A, Authority, of the standard describes three categories of limitations for use:
  - a. Specific Prohibitions: Specific classes of entities for which the use of the 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.
  - b. Qualitative characteristics of a less complex entity to determine if use of the ISA for LCE is appropriate: The qualitative characteristics are to be considered both individually and in combination. If there is uncertainty about whether the characteristics in the Authority apply, the use of the ISA for LCE may not be appropriate. (i.e. if in doubt, you are out). The qualitative characteristics are not exhaustive nor absolute (including numerical indicators). The qualitative characteristics are outlined in Part A of the standard.
  - c. A Quantitative threshold to further limit the applicability of the standard. National standard setting authorities may set quantitative thresholds to exclude audits of entities to be conducted using the ISA (NZ) for LCE. Professional judgement is needed to determine whether the ISA (NZ) for LCE is appropriate for use.
13. Regarding specific prohibitions, the XRB proposed an additional prohibition stating that the ISA (NZ) for LCE may not be used to audit FMC reporting entities considered to have higher level of public accountability (FMC HLPAs). 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).
14. We considered whether other FMC reporting entities, i.e., those considered to have a lower level of public accountability (FMC LLPAs) should be prohibited but noted that there may be entities in this category that are less complex. FMC LLPAs that have characteristics of complexity would be scoped out through the qualitative characteristics in the Authority.
15. Respondents were supportive for the proposed specific prohibition in the standard for FMC HLPAs reporting entities. Therefore, this prohibition has been added to paragraph A.1.(c) of the ISA (NZ) for LCE.
16. The qualitative characteristics were set by the IAASB. The XRB did not consider any need to amend what has been set, as they appear to be appropriate for use in New Zealand.
17. Regarding implementing a quantitative threshold, the XRB considered various 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 in New Zealand because:

- a. a quantitative threshold is not necessarily an indicator of complexity.
  - b. there could be undue audit effort in testing the accuracy of metrics used in the calculation of quantitative thresholds before determining whether the use of ISA (NZ) for LCE is appropriate.
  - c. the specific prohibitions and qualitative characteristics will already scope out entities which have characteristics of complexity.
18. Respondents supported this approach, and therefore we have not added a quantitative threshold to the ISA (NZ) for LCE.

### The addition of Part 11, audit of service performance information

19. In New Zealand, many Public Benefit Entities (PBEs) 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 SPI, audited. As many of these PBEs may be less complex entities, the XRB proposed adding a part to the ISA (NZ) for LCE to include requirements for auditing SPI of a less complex entity. This was included as Part 11 *Audit of Service Performance Information* in the Exposure Draft.
20. The XRB developed the requirements of Part 11, with reference to the approach in NZ AS 1 (Revised), but tailored and proportionate to an audit of a less complex entity. It is written to follow the flow of an audit of SPI. The requirements still enable the auditor to provide reasonable assurance. We used the drafting principles set by the IAASB to be:
- a. Clear - meaning drafted in an easy to understand and unambiguous way.
  - b. Understandable - avoiding unnecessary words and elements and by using plain language.
  - c. Concise - avoiding unnecessary repetition.
21. Part 11 is used in conjunction with Parts 1-10 of the ISA (NZ) for LCE. Paragraph NZP.0. notes that for the purposes of the standard, references to “financial statements” include “service performance information” and “entity information” where relevant.
22. Respondents were asked:
- a. Whether they support the addition of Part 11 to enable the audit of SPI.
  - b. Whether the requirements and EEM in Part 11 are appropriately tailored for LCEs, and are there requirements in Parts 1-10 that would be difficult to apply and should be refined.
23. The majority of respondents supported the addition of Part 11, noting that the requirements and EEM was appropriately tailored for LCEs.
24. We are aware of the challenges around the reporting and assurance of service performance information. The XRB is being proactive in addressing these challenges, and has an active project to support both the preparation and assurance of the statement of service performance.
25. We received suggestions for further clarification of requirements and EEM as follows:
- a. It was suggested that the EEM wording at paragraph 11.1.1. about the objectives should be clearer and more concise, and refer to Part 11.5 on the auditor’s evaluation



of whether service performance information is appropriate and meaningful. We agreed and made changes to the paragraph.

- b. It was suggested that the requirement at paragraph 11.7.2.(b) clarify that the auditor determines the relevant assertions and related performance measures, descriptions, or disclosures that are appropriate and meaningful. We agreed and made changes to the paragraph. We clarified the materiality requirements at paragraph 11.6.3. to clarify how the auditor applies materiality and changed the paragraph to be a requirement.
- c. It was suggested that EEM wording at paragraph 11.7.2. referring to inherent risk assessment being conducted at a *meaningful level* because of the aggregation, measurement and presentation of service performance information may be confused with the term appropriate and meaningful. It was also suggested that content was added to guide auditors on inherent risk factors to consider when undertaking an inherent risk assessment. We agreed and made changes to the EEM.
- d. It was suggested that the EEM wording at paragraph 11.9.1. be clarified in relation to attribution and sufficient appropriate audit evidence. We agreed and made changes, adding titles to denote the sections relating to: sources of information, internal sources, sufficiency and appropriateness of audit evidence, and attribution of SPI. We also added guidance on the attribution of SPI, when multiple entities contribute to an element/aspect of service performance.
- e. It was suggested that the requirement at paragraph 11.13.4. be reworded to remove the words “in extremely rare circumstances” where service performance information is misleading, as there could be more than an extremely rare possibility that SPI could be misleading. We agreed and removed the words.

### In-house legal counsel

- 26. We also received a suggestion to add a NZ requirement (paragraph NZ 10.1) from ISA (NZ) 501 *Audit Evidence – Specific Considerations for Selected Items* for when an LCE utilises in-house legal counsel, for the auditor to obtain a legal letter from the in-house level counsel. While it may be uncommon for LCEs to have in-house legal counsel we acknowledge that there still may be entities that have them, and therefore the ISA (NZ) for LCE should have consistent requirements with ISA (NZ) 501. Therefore, we added para. NZ 7.4.24.1. to require a written representation from in-house legal counsel when the in-house legal counsel has the primary responsibility for litigation and claims and is in the best position to corroborate representations from management and those charged with governance.

### NZ specific amendments to the ISA for LCE and consequential amendments to the ISAs (NZ)

- 27. The XRB proposed minor amendments to harmonise the ISA for LCE with local principles and practices, as reflected in the ISAs (NZ). The amendments do not result in a standard that conflicts with, or results in lesser requirements. In summary, the amendments relate to:
  - Responsibilities for the financial statements being those of governance rather than management, including in requirements relating to the engagement letter, auditor’s report, and written representations. (Ref: Para. NZ4.2.1., NZ8.6.7. and others)



- Reference to the specific NZ financial reporting frameworks and 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.
28. Each amended requirement paragraph or amended EEM in the ISA (NZ) for LCE is prefixed by "NZ". Amended requirement paragraphs have "[Amended by the NZAuASB]" to indicate that the paragraph differs from the international equivalent.
29. The XRB has also made 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
30. We requested comments on the proposed NZ specific amendments and the conforming amendments, respondents were supportive of the amendments, there were no disagreements received on what was proposed.

### Application date

31. There was general support for the proposed application date of periods beginning on or after 15 December 2025. The standard would be available for use and only applicable if the entity being audited meets the specific criteria set out in Part A of the standard.

## Guidance

32. The IAASB has issued the following guidance documents:
- a. [Adoption guide](#)
  - b. [Auditor reporting](#)
  - c. [Authority of the standard](#)
  - d. [Basis for conclusions](#)
  - e. [Fact sheet](#)
  - f. [FAQs](#)
  - g. [First time implementation guide](#)

33. We intend to issue a guidance document on auditor reporting, applicable to NZ circumstances, in due course.
34. We welcome any further comments or suggestions on guidance auditors would find useful as they implement the standard.
35. We intend to conduct a post implementation review of the ISA (NZ) for LCE in a few years following implementation. We welcome feedback as auditors start to apply the ISA (NZ) for LCE and will look for ways to facilitate sharing experiences and learnings with others.

