STANDARD FOR AUDITS OF SMALL ENTITIES

DRAFT – JUNE 4TH 2015

NRF

Contents

PREFACE

This standard is a principles based, stand-alone auditing standard, tailored specifically to audits of the financial statements of small entities.

An audit in accordance with this standard will provide the auditor with reasonable assurance about whether the financial statements of a small entity are free from material misstatements. The audit evidence obtained will provide the basis for an audit report stating the auditor's opinion.

The standard has been developed based on general auditing principles and use a risk based audit approach. The application of the standard requires the auditor's judgment and professional skepticism.

The standard requires the auditor to assess the risks of material misstatements in the financial statements and to plan and perform audit procedures to reduce that risk to an acceptable level.

When applying this standard the auditor shall comply with relevant ethical requirements, including those pertaining to independence, and with the requirements of The International Standard on Quality Control (ISQC 1).

The standard is applicable for audits of small entities below the mandatory audit threshold in the EU accounting directive.

1 GENERAL PRINCIPLES AND RESPONSIBILITIES

1.1 OVERALL OBJECTIVES

The overall objectives of the auditor when conducting an audit of financial statements are:

- to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and
- to report on the financial statements, and communicate, in accordance with the auditor's findings.

1.2 SUPERVISION AND QUALITY CONTROL

The engagement partner shall take responsibility for the overall quality on each audit engagement. Throughout the engagement, the engagement partner shall remain alert, through observation, inspection of audit documentation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements and professional standards.

The engagement partner shall take responsibility for:

- the direction, supervision and performance of the audit engagement in compliance with this standard, International Standards on Quality Control, relevant ethical requirements and applicable legal and regulatory requirements;
- reviews being performed in accordance with the firm's policies and procedures;
- sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor's report to be issued;
- consultations being made in accordance with the firms policies and procedures on difficult or contentious matters and when there are differences of opinions in the engagement team;
- an engagement quality control review being performed in accordance with the firm's policies and procedures; and
- the auditor's report being appropriate in the circumstances.

1.3 PERFORMING THE AUDIT

When performing the audit of the financial statement the auditor shall;

- comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements;
- plan and perform the audit with professional skepticism recognizing that circumstances may exist that cause the financial statements to be materially misstated;
- exercise professional judgment in planning and performing the audit of the financial statements;
- 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; and
- conduct the audit in accordance with this audit standard.

1.4 AUDIT EVIDENCE

When obtaining information to be used as audit evidence, the auditor shall consider the relevance and reliability of the information. The source of the information, original vs. copy and written vs. oral information, influence the auditor's considerations of the reliability.

When using information produced by the entity, the auditor shall evaluate the accuracy and completeness of the information, and whether the information is sufficiently precise and detailed for the auditor's purposes.

When using information prepared by management's experts, external experts or other auditors, the auditor shall, to the extent necessary:

- evaluate the competence, capabilities and objectivity of those who have prepared the information;
- consider the need for direct communication or other appropriate actions with the expert or other auditor; and
- evaluate whether the auditor can rely on the information as audit evidence.

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.

If the auditor during the audit identifies exceptions, differences or non-compliance, the auditor shall consider the impact to the audit and consider modifications or additions to the audit procedures.

The auditor shall determine what modifications or additions to audit procedures are necessary to resolve any inconsistencies or doubts, and shall consider their effect on other aspects of the audit and document how the auditor addressed the inconsistency, if:

- audit evidence obtained from one source is inconsistent with that obtained from another;
- the auditor has doubts over the reliability of information to be used as audit evidence;
- if responses to inquiries of management or those charged with governance are inconsistent; and
- if the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter.

1.5 DOCUMENTING THE ENGAGEMENT

The auditor shall prepare documentation that provides:

- a sufficient and appropriate record of the basis for the auditor's report; and
- evidence that the audit was planned and performed in accordance with this standard and applicable legal and regulatory requirements.

1.5.1 Documentation Requirements

The auditor shall prepare audit documentation on a timely basis that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

- the nature, timing and extent of the audit procedures planned and performed to comply with this standard and applicable legal and regulatory requirements, including significant changes made during the audit;
  - who performed the work and when, and
  - who performed the review and when.
- the results of the audit procedures performed, and the audit evidence obtained, including the characteristics of the specific items or matters tested; and

- significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

Where matters arise that are required by this standard to be communicated with management, and those charged with governance, the auditor shall include them, and when and to whom they were communicated, in the audit documentation. 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.

1.5.2 Assembly of the Final Audit File

The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. After the assembly of the final audit file, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period. If the auditor finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, the auditor shall, regardless of the nature of the modifications or additions, document: the specific reasons for making them; and when and by whom they were made and reviewed

1.6 COMMUNICATION WITH MANAGEMENT AND THOSE CHARGED WITH GOVERNANCE

The auditor shall communicate with management, and those charged with governance, on a timely basis. Matters to be communicated include;

- significant findings from the audit;
  - the auditor's views about qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures.
  - identified control deficiencies
  - identified misstatements
  - identified fraud or information that indicates that a fraud may exist
  - identified or suspect non-compliance with laws or regulations with relevance for the audit
- modifications to, emphasis of matter and other matters in the auditor's report;
- communication requirements in laws and regulation;
- other matters, if any, arising from the audit that, in the auditor's professional judgment, are significant to the financial statements and the financial reporting process.

The auditor shall use professional judgment in determining the appropriate form of communicating with management and those charged with governance. When determining the form of communication, oral vs. written, the auditor shall consider;

- legal requirements for communication
- the significance of the matters to be communicated
- other matters when oral communication would not be adequate

2 ACCEPTANCE OR CONTINUANCE OF AN AUDIT ENGAGEMENT

2.1 OBJECTIVE

The objective of the auditor is to evaluate whether to accept or continue an audit engagement.

2.2 PRECONDITIONS FOR AN AUDIT

The auditor shall consider whether the preconditions for an audit are present. In making this consideration the auditor evaluates whether;

- the financial reporting framework to be applied in the preparation of the financial statements is acceptable;
- management will provide the auditor with:
  - all information of which management is aware that is relevant
  - any additional information that the auditor may request from management
  - unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.
- the terms of engagement is acceptable;
- management or those charged with governance impose a limitation on the scope of the auditor’s work; and
- there are other factors that may affect the engagement.

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

Unless management’s responsibilities for the financial statement and the scope of the audit is clearly defined in applicable law or regulation, the auditor shall obtain from management or those charged with governance, as appropriate, an written agreement:

- that it acknowledges and understands its responsibility:
  - for the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;
  - for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
  - to provide the auditor with:
    - access to all information of which management is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
    - additional information that the auditor may request from management for the purpose of the audit; and
    - unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

- of the terms of the audit engagement, including:
    - the objective and scope of the audit
    - the responsibilities of the auditor
    - the responsibilities of management
    - identification of the applicable financial reporting framework
    - reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

2.3 ADDITIONAL DOCUMENTATION REQUIREMENTS

In addition to the general documentation requirements **(ref. 1.5)** for an audit engagement, the auditor shall include the following in the audit documentation:

- issues identified with respect to compliance with relevant ethical requirements, and how they were resolved;
- conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the audit firm that support these conclusions;
- conclusions reached regarding the acceptance and continuance of client relationships and audit engagements; and
- the nature and scope of, and conclusions resulting from, consultations undertaken during the course of the audit engagement.

3 PLANNING

3.1 OBJECTIVE

The objective of the auditor is to plan the audit to be performed in an effective manner and to apply the concept of materiality appropriately during the course of the audit.

3.2 SCOPE, TIMING AND DIRECTION

The auditor shall set the scope, timing and direction of the audit that supports the development of the audit. In establishing the scope, timing and direction of the audit, the auditor considers:

- the characteristics of the engagement;
- the expected timing of the audit and the nature of the communications and reporting required;
- factors that, in the auditor's professional judgment, are significant in determining the audit strategy;
- the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements for this entity is relevant; and
- the nature, timing and extent of resources necessary to perform the audit.

3.3 DETERMINING MATERIALITY

The auditor shall determine materiality for the financial statements as a whole. The auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements. In general, misstatements, including omissions, are considered to be material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions taken by the users, based on the financial statements.

If the auditor becomes aware of information during the audit that would have caused the auditor to determine a different materiality level, the materiality level shall be revised.

3.4 ADDITIONAL DOCUMENTATION REQUIREMENTS

In addition to the general documentation requirements **(ref. 1.5)** for an audit engagement, the auditor shall include the following in the audit documentation:

- the scope, timing and direction of the audit, and significant changes made during the audit.
- the materiality, including any revisions, for the financial statements as a whole, and judgments made in determining materiality.

4 RISK ASSESSMENT

4.1 OBJECTIVE

The objective of the auditor is to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels. This is achieved through obtaining an understanding of the entity and its environment, including the entity's internal controls, and thereby providing a basis for designing responses to the assessed risks of material misstatement.

4.2 RISK ASSESSMENT PROCEDURES AND RELATED ACTIVITIES

The auditor shall perform risk assessment procedures to obtain an understanding of the entity and its environment and to enable the auditor to identify and assess the risks of material misstatement at the financial statement and assertion levels. This forms the basis for designing the procedures to be performed in response to assessed risks (further audit procedures). Throughout the audit, the auditor shall remain alert for evidence of events or changes of circumstances that may affect existing, or identify new risks.

The risk assessment procedures shall include:

- discussions with management and others within the entity who in the auditor's judgment may have information that is likely to assist in identifying risks of material misstatement due to fraud or error;
- analytical procedures to identify unusual or unexpected trends and relationships that may indicate risks of material misstatement due to fraud or error; and
- observation and inspection.

In addition, the risk assessment procedures shall include those procedures deemed necessary, using professional judgment, to be able to;

- identify potential fraud risk, including the risk of management override of controls and fraud related to revenue recognition, also when no fraud risk factors have been identified;
- assess whether the entity may have entered into agreements or relationships that may result in unrecognized liabilities, future commitments or changes to current asset valuations;
- assess whether transactions, events or conditions exist that may give rise to the need for accounting estimates to be recognized or disclosed in the financial statements. When an estimate is assessed to be significant for an item in the financial statements, the auditor shall obtain an understanding of the assumptions and methods used in determining the estimate;
- assess the entity's ability to continue as a going concern;
- identify risks related to non-compliance with laws and regulations that may have a material effect on the financial statements; and
- identify the entity's related parties, and if applicable
  - understand the nature of the relationships between the entity and the related parties; and
  - identify and understand the nature and purpose of any transactions with the related parties.

4.3 UNDERSTANDING OF THE ENTITY AND ITS ENVIRONMENT

To be able to identify and assess the risks of material misstatement at the financial statement and assertion levels the auditor shall obtain an understanding of;

- external factors affecting the entity's objectives and strategies, and those related business risks that may result in risks of material misstatement (including accounting estimates and going concern assumption). External factors include industry, regulatory, and other factors (such as the applicable financial reporting framework)
- the nature of the entity, including operations, ownership and governance structures, investment plans, structure and financing, to enable the auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements.
- the entity's selection and application of accounting policies, including the reasons for changes thereto. The auditor shall evaluate whether the entity's accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry.
- the entity's control environment relevant to financial reporting, including consideration related to;
  - the governance and management functions;
  - the attitudes, awareness, and actions of those charged with governance and management concerning the entity's internal control and its importance in the entity;
  - the owner-managements active involvement influencing the risks arising from lack of segregation of duties and management override of controls;
  - that the control environment in itself does not prevent, or detect and correct, a material misstatement.
- the information system relevant to financial reporting, including;
  - For significant classes of transactions the auditor shall obtain an understanding on how those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements
  - How the information system captures events and conditions, other than transactions, that are significant to the financial statements;
  - The financial reporting process used to prepare the entity's financial statements, including significant accounting estimates and disclosures; and journal entries, including non-standard journal entries used to record non-recurring, unusual transactions or adjustments.
- relevant control activities, evaluate the design and determine whether the controls have been implemented, if the auditor plan to rely on identified control activities.

4.4 IDENTIFYING AND ASSESSING THE RISK OF MATERIAL MISSTATEMENT

4.4.1 Risk assessment

The auditor shall identify and assess the risks of material misstatement at:

- the financial statement level; and
- the assertion level for classes of transactions, account balances, and disclosures,

to provide a basis for designing and performing further audit procedures.

For this purpose, the auditor shall:

- identify risks, whether due to fraud or error, throughout the process of obtaining an understanding of the entity and its environment, including the control environment and information system, and by considering the classes of transactions, account balances, and disclosures in the financial statements;
- assess the identified risks, and evaluate whether they relate pervasively to the financial statements as a whole and potentially affect many assertions;

- relate the identified risks to what can go wrong at the assertion level, taking account of relevant controls that the auditor intends to test; and
- consider the likelihood of misstatement, including the possibility of multiple misstatements, and whether the potential misstatement is of a magnitude that could result in a material misstatement.

4.4.2 Risks that require special consideration

As part of the risk assessment the auditor shall determine whether any of the risks identified are, in the auditor's judgment, a significant risk. In exercising this judgment, the auditor shall exclude the effects of identified controls related to the risk.

In exercising judgment as to which risks are significant risks, the auditor shall consider at least the following:

- whether the risk is a risk of fraud;
- whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;
- the complexity of transactions;
- whether the risk involves significant transactions with related parties. The auditor shall treat identified significant related party transactions outside the entity's normal course of business as giving rise to significant risks;
- the degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and
- whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual.

4.4.3 Reassessment of risk

The auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained. In circumstances where the auditor obtains audit evidence from performing further audit procedures, or if new information is obtained, either of which is inconsistent with the audit evidence on which the auditor originally based the assessment, the auditor shall revise the assessment and modify the further planned audit procedures accordingly.

4.5 ADDITIONAL DOCUMENTATION REQUIREMENTS

In addition to the general documentation requirements **(ref. 1.5)** for an audit engagement, the auditor shall include the following in the audit documentation of the auditor's understanding of the entity and its environment and the assessment of the risks of material misstatement:

- key elements of the understanding obtained regarding each of the aspects of the entity and its environment and of the control environment, information system and the sources of information;
- the names of the identified related parties and the nature of the related party relationships;
- the identified and assessed risks of material misstatement, including risk due to fraud, at the financial statement level and at the assertion level;
- the controls related to identified risks of which the auditor has obtained an understanding; and
- identified or suspected non-compliance with laws and regulations and the results of discussion with management and, where applicable, those charged with governance and parties outside the entity.

5 THE AUDITOR´S RESPONSE TO ASSESSED RISKS

5.1 OBJECTIVE

The objective of the auditor is to obtain sufficient and appropriate audit evidence regarding the assessed risks of material misstatement, through appropriate responses to those risks. Further audit procedures are test of controls, substantive procedures or a combination. The auditor shall use professional judgement in designing and performing further audit procedures that are considered most efficient in response to the identified and assessed risks.

5.2 AUDIT PROCEDURES RESPONSIVE TO THE ASSESSED RISKS OF MATERIAL MISSTATEMENT AT THE ASSERTION LEVEL

The auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level. This forms the basis for designing further audit procedures. When performing further audit procedures at an interim date, the auditor shall consider additional procedures for the remaining period.

In designing the further audit procedures, the auditor shall:

- consider the reasons for the assessment given to the risk of material misstatement at the assertion level for each class of transactions, account balance, and disclosure, including:
    - the likelihood of material misstatement due to the particular characteristics of the relevant class of transactions, account balance, or disclosure (that is, the inherent risk); and
    - whether the risk assessment takes account of relevant controls (that is, the control risk), thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively (where the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); and
- obtain more persuasive audit evidence the higher the auditor’s assessment of risk.

5.2.1 Tests of Controls

When the auditor plan to rely on controls, the auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of those controls that the auditor intends to rely on.

In designing and performing tests of controls, the auditor shall obtain more persuasive audit evidence the greater the reliance the auditor places on the effectiveness of a control.

Considerations when performing test of controls:

- nature and extent of the controls
    - the period covered and how often the control has been performed
    - significant changes in the controls in the period
    - determine whether the controls to be tested depend upon other controls (indirect controls)
- timing of the test of controls
    - test controls for a selected period, or throughout the whole period
    - if only testing for a selected period, determine additional procedures for the period that are not tested

- evaluating the operating effectiveness of controls
  - the cause and potential consequences of any deviations detected
  - whether misstatements detected while performing substantive procedures indicate that controls are not operating effectively
  - the need for additional test of controls or other procedures to obtain appropriate audit evidence
  - whether the tests of controls that have been performed provide an appropriate basis for reliance on the controls

5.2.2 Substantive procedures

Substantive procedures are audit procedures designed to detect material misstatements at the assertion level. Based on the auditor's judgment substantive procedures are performed by testing the details of the transaction, disclosure or account balance, substantive analytical procedures or a combination of those.

Substantive procedures are designed and performed in response to assessed risks **(4.4)** in order to obtain sufficient and appropriate audit evidence at the assertion level. Irrespective of the assessed risks, substantive procedures shall be performed for each material class of transactions, account balance, and disclosure. Substantive procedures in response to identified significant risks shall be specifically designed to respond to that risk and those procedures shall include tests of details.

Further audit procedures in response to assessed risks shall always include substantive procedures:

- to obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements;
- to address the risks of management override of controls;
- to address the risk caused by any identified events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, including
  - evaluating management's plans for future actions in relation to its going concern assessment;
  - evaluate managements cash flow forecast, and analyze significant factors affecting management's plans for future action;
  - consider whether any additional facts or information have become available since the date on which management made its assessment; and
  - request written representations from management and, where appropriate, those charged with governance, regarding their plans for future action and the feasibility of these plans;
- as a retrospective review of management judgments and assumptions in relation to significant accounting estimates reflected in prior years financial statements; and
- in relation to the financial statement closing process for
  - agreeing or reconciling the financial statements with the underlying accounting records;
  - examining material journal entries and other adjustments made during the course of preparing the financial statements; and
  - evaluating whether the overall presentation of the financial statements, including the related disclosures, is in accordance with the applicable financial reporting framework.

Considerations when designing substantive procedures to address risks identified in **4.4**:

- Fraud risk
  - the appropriateness of journal entries in the general ledger and other adjustments made in the preparation of the financial statements;
  - whether there is a need to test journal entries in the general ledger and other adjustments made throughout the period, and
  - the business rationale for significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual.
- Going concern
  - management's assessment as to the entity's ability to continue as a going concern;
  - covenants or other circumstances that may affect management in their assessment;
  - whether any additional facts or information have become available since the date on which management made its assessment; and
  - when material uncertainty exist, the effect this may have on fraud risk, including managements involvement in the preparation of accounting estimates and in applying accounting policies.
- Laws and regulations
  - applicable laws and regulations.
- Accounting estimates
  - the method used and consistency in the method used by management in preparing the accounting estimate, input and assumptions on which it is based, including estimation uncertainty;
  - historical accuracy in estimates made by management in prior periods;
  - potential biases in the estimates and an evaluation whether the circumstances producing the bias, if any, represents a risk of material misstatement due to fraud; and
  - whether events occurring up to the date of the auditor's report provide audit evidence regarding the accounting estimate.
- Related parties
  - arrangements or information suggesting the existence of related party relationships or transactions that management has not previously identified or disclosed to the auditor;
  - the business rationale for significant transactions involving related parties; and
  - the terms of transactions.

5.2.2.1 Substantive analytical procedures

When designing and performing substantive analytical procedures to address assessed risks at assertion level the auditor shall:

- evaluate the reliability of data used in the analyses;
- develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify misstatements;
- determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation as required; and
- for identified differences exceeding acceptable levels, use professional judgment when investigating such differences and performing additional audit procedures as necessary in the circumstances

5.2.2.2 Test of details

When performing test of details to address assessed risks at assertion level the auditor shall, using professional judgment, design the nature, timing and the extent of the procedure to identify the misstatements and reduce the audit risk to an acceptable level. A test of details can be performed by inspections, recalculation or external confirmations. When selecting items for a test of details the auditor can either select all items, specific items or base the selection of items on audit sampling techniques.

When performing audit sampling the auditor shall determine the sample size sufficient to reduce the risk to an acceptably low level and select items in a way that each sampling unit in the population has a chance of selection. Identified misstatements in the sample shall be investigated as to their nature and cause, and their effect on the audit. Misstatements in the sample, excluding misstatements that do not affect the remaining population, shall be projected to the population.

When performing external confirmations the auditor shall determine the extent of confirmations, select the confirming parties, send the requests and receive the responses directly from the confirming party. The auditor shall maintain control over the external confirmations and follow up on the confirming party when applicable.

5.3 EVALUATION

When the auditor has performed the audit procedures designed to respond to the assessed risks of material misstatement at the assertion level, evaluations shall be made as to the whether sufficient appropriate audit evidence is obtained for relevant assertions, including evaluation of identified misstatements.

5.3.1 Evaluation of misstatements identified during the audit

Throughout the audit, the auditor shall accumulate misstatements identified, other than those that are clearly trivial. The auditor shall determine the nature and cause of each identified misstatement, including whether the misstatements may indicate fraud, and their potential effect on the risk assessment and the audit strategy.

The auditor shall communicate on a timely basis all misstatements accumulated during the audit with the appropriate level of management, and where appropriate, those charged with governance, and request those misstatements to be corrected. If some or all of the misstatements are not corrected, the auditor shall obtain an understanding of the reasons for not making the corrections and shall consider that understanding when evaluating whether the financial statements as a whole are free from material misstatement.

The auditor shall determine whether uncorrected misstatements are material, individually or in aggregate. In making this determination, the auditor shall consider:

- the size and nature of the misstatements, both in relation to particular classes of transactions, account balances or disclosures and the financial statements as a whole, and the particular circumstances of their occurrence;
- the potential reaction of the misstatements form the users of the financial statement; and
- the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.

The auditor shall communicate with management and, where appropriate, those charged with governance whether they believe the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole.

5.3.2 Evaluating the Sufficiency and Appropriateness of Audit Evidence

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

The auditor shall conclude whether sufficient appropriate audit evidence has been obtained. When evaluating the sufficiency of the audit evidence the auditor shall consider if the nature and cause of identified misstatements indicate that other misstatements may exist that when aggregated could be material.

In forming an opinion, the auditor shall consider all relevant audit evidence, regardless of whether it appears to corroborate or to contradict the assertions in the financial statements.

If the auditor has not obtained sufficient appropriate audit evidence as to a material financial statement assertion, the auditor shall attempt to obtain additional audit evidence. If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall express a qualified opinion or issue a disclaimer on the financial statements.

5.4 ADDITIONAL DOCUMENTATION REQUIREMENTS

In addition to the general documentation requirements **(ref. 1.5)** for an audit engagement, the auditor shall include the following in the audit documentation of the auditor's responses to the assessed risks of material misstatement:

- the connection between the procedures performed and the assessed risks at the assertion level; and the results of the audit procedures, including the conclusions where these are not otherwise clear;
- all misstatements accumulated during the audit and whether they have been corrected ;
- the basis for the auditor's conclusions about:
    - whether uncorrected misstatements are material, individually or in aggregate;
    - the reasonableness of accounting estimates and their disclosure that give rise to significant risks and indicators of possible management bias, if any;
    - the going concern assumption;
    - the compliance with laws and regulations;
    - the fraud risk
- the related party transactions and their disclosure that give rise to significant risks, if any; and
- evidence that the financial statements agree or reconcile with the underlying accounting records.

6 CONCLUDING AND REPORTING

6.1 OBJECTIVES

The objective of the auditor, is to evaluate the audit evidence obtained, identified misstatements and the entity's application of the financial reporting framework and to conclude whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

6.2 SUBSEQUENT EVENTS

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

The auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, if the auditor becomes aware of facts or events that may have an impact on the auditor's conclusion:

- after the date of the auditor's report but before the financial statements are issued, or
- after the financial statements have been issued,

the auditor shall perform additional procedures and evaluate the impact on the auditor's report.

6.3 ANALYTICAL PROCEDURES THAT ASSIST WHEN FORMING AN OVERALL CONCLUSION

The auditor shall design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity.

6.4 WRITTEN REPRESENTATION

The auditor shall evaluate the need to obtain written representations to confirm certain matters or to support other audit evidence relevant to the financial statements or one or more specific assertions in the financial statements. When evaluating the need for written representation, the auditor considers;

- the extent of audit evidence obtained by oral representation;
- existence of material uncertainty for going concern;
- estimates with high degree of estimation uncertainty;
- existence of related parties and related party transactions; and
- if managements responsibility for the preparation of the financial statement in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation is defined in law or covered in other ways.

Unless the responsibility for the preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation is clearly defined in law or covered in other way, for example by managements signature on the financial statements, the auditor shall obtain written representation on this matter.

The date of the written representations shall be as near as practicable to, but not after, the date of the auditor's report on the financial statements.

6.5 FORMING AN OPINION ON THE FINANCIAL STATEMENTS

The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

In order to form that opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error.

The conclusion shall take into account:

- whether sufficient appropriate audit evidence has been obtained,
- whether uncorrected misstatements are material, individually or in aggregate,
- whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework, including
    - the entities application of the requirements of the applicable financial reporting framework,
    - the qualitative aspects of the entity's accounting practices,
- if the financial statements are prepared in accordance with a fair presentation framework, whether the financial statements are fairly presented.

6.6 FORM OF OPINION

The auditor shall express an unmodified opinion when the auditor concludes that the financial statements are prepared and fairly presented, in all material respects, in accordance with the applicable financial reporting framework. If the financial statements is prepared in accordance with the requirements of a fair presentation framework, the auditor shall also express an opinion whether the financial statement are fairly presented.

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

- concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or, where applicable, the financial statements do not achieve fair presentation; or
- is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

When modifying the opinion the auditor provides;

- a qualified opinion when the auditor:
    - concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or
    - is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.
- an adverse opinion when the auditor concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.
- a disclaimer of opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to form an audit opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

The auditor shall, if considered necessary:

- draw the users' attention to a matter presented or disclosed in the financial statements, include an Emphasis of Matter paragraph in the auditor's report.
- communicate a matter other than those that are presented or disclosed in the financial statements , include an Other Matter paragraph in the auditor's report.

6.7 AUDITOR´S REPORT

The auditor's report shall be in writing and shall[1]:

- identify the entity subject of the audit; specify the financial statements and the date and period covered; and identify the financial reporting framework that has been applied in the preparation;
- include a description of the scope of the statutory audit which shall, as a minimum, identify the auditing standards in accordance with which the statutory audit was conducted;
- include an audit opinion, which shall be either unqualified, qualified or an adverse opinion and shall state clearly the opinion as to:
    - whether the annual financial statements give a true and fair view in accordance with the relevant financial reporting framework, or
    - whether the annual financial statement are prepared, in all material respects, in accordance with the applicable financial reporting framework; and,
    - where appropriate, whether the annual financial statements comply with statutory requirements.
    - If the auditor is unable to express an audit opinion, the report shall contain a disclaimer of opinion;
- refer to any other matters or emphasis of matter paragraphs to which the auditor draw attention without qualifying the audit opinion;
- provide a statement on any material uncertainty relating to events or conditions that may cast significant doubt about the entity's ability to continue as a going concern;
- be signed;
- be dated, the date shall be no earlier than the date on which the auditor obtained sufficient appropriate audit evidence; and
- identify the place of establishment of the statutory auditor(s) or the audit firm(s).

6.7.1 Content of the Auditor's Report When the Opinion Is Modified

When the auditor modifies the audit opinion, qualified opinion, adverse opinion or disclaimer of opinion, the auditor shall;

- include a section in the auditor's report with the heading "Qualified Opinion," "Adverse Opinion," or "Disclaimer of Opinion," as appropriate. This section shall include;
    - when expressing a qualified or adverse opinions, a description of the basis for the qualification, including;
        - for misstatements relating to specific amounts, a description and quantification of the financial effects of the misstatement, unless

[1] Depending on regulatory requirements there might be additional reporting requirements, such as;

- , express an opinion on:
    - whether the management report is consistent with the financial statements for the same financial year, and
    - whether the management report has been prepared in accordance with the applicable legal requirements;
- if applicable, state whether, in the light of the knowledge and understanding of the undertaking and its environment obtained in the course of the audit, he, she or it has identified material misstatements in the management report, and shall give an indication of the nature of any such misstatements.

    impracticable. If it is not practicable to quantify the financial effects, this shall be stated;
    - for misstatements relating to narrative disclosures, a description on how the disclosure is misstated;
    - for misstatements relating to non-disclosures, a description of the nature of the omitted information, and, unless prohibited by law, include the omitted disclosure; or
  - when expressing a qualified opinion or a disclaimer of opinion as a result of inability to obtain sufficient appropriate audit evidence, the reason for the inability.
- when expressing a qualified or adverse opinion, amend the statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion;
- when disclaiming an opinion of the financial statement, not include in the auditor's report descriptions of the auditors responsibility and state whether sufficient and appropriate audit evidence is obtained; and
- when expressing the opinion;
  - with a qualification, state that, in the auditor's opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion section, the financial statement , in the auditor's opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion section,
    - the accompanying financial statements present fairly, in all material respects (or give a true and fair view of) [...] in accordance with [the applicable financial reporting framework]; or as applicable,
    - the accompanying financial statements have been prepared, in all material respects, in accordance with [the applicable financial reporting framework].
  - with an adverse opinion, state in the auditor's opinion, that because of the significance of the matter(s) described in the Basis for Adverse Opinion section:
    - the accompanying financial statements do not present fairly (or give a true and fair view of) [...] in accordance with [the applicable financial reporting framework]; or as applicable
    - "the accompanying financial statements have not been prepared, in all material respects, in accordance with [the applicable financial reporting framework].
  - with a disclaimer of opinion, state that
    - the auditor does not express an opinion on the accompanying financial statements, and
    - because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements.

Appendix 1. Sample audit report

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of ABC Company [or Other Appropriate Addressee]

Opinion on the Audit of the Financial Statements and the Management Report

We have audited the accompanying financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement [and cash flow statement] for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Company as at December 31, 20X1, and (*of*) its financial performance and its cash flows for the year then ended in accordance with *(insert Financial Reporting Framework)*.

[2]

Scope

We conducted our audit in accordance with laws, regulations, and auditing standards and practices generally accepted in (*xyz country*), including Standard for Audits of Small Entities. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

[Auditor Address]

[*Date*]

[2] In addition, according to the EU auditing directive the audit report shall include: "Based on our audit of the financial statements, it is our opinion that the information presented in the Management Report concerning the financial statements is consistent with the financial statements and is prepared in accordance with (*insert applicable law and regulations*)."

Appendix 2. Glossary

Accounting estimate: An approximation of a monetary amount in the absence of a precise means of measurement. This term is used for an amount measured at fair value where there is estimation uncertainty, as well as for other amounts that require estimation.

Accounting records: The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in formal journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures.

Analytical procedures: Evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

Applicable financial reporting framework: The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

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

Assertions: Representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur. Assertions used by the auditor to consider the different types of potential misstatements that may occur fall into the following three categories and may take the following forms:

a) Assertions about classes of transactions and events for the period under audit:
    i. *Occurrence*—transactions and events that have been recorded have occurred and pertain to the entity.
    ii. *Completeness*—all transactions and events that should have been recorded have been recorded.
    iii. *Accuracy*—amounts and other data relating to recorded transactions and events have been recorded appropriately.
    iv. *Cutoff*—transactions and events have been recorded in the correct accounting period.
    v. *Classification*—transactions and events have been recorded in the proper accounts.
b) Assertions about account balances at the period end:
    i. *Existence*—assets, liabilities, and equity interests exist.
    ii. *Rights and obligations*—the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
    iii. *Completeness*—all assets, liabilities and equity interests that should have been recorded have been recorded.
    iv. *Valuation and allocation*—assets, liabilities, and equity interests are included in the financial statements at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.

c) Assertions about presentation and disclosure:
   i. *Occurrence and rights and obligations*—disclosed events, transactions, and other matters have occurred and pertain to the entity.
   ii. *Completeness*—all disclosures that should have been included in the financial statements have been included.
   iii. *Classification and understandability*—financial information is appropriately presented and described, and disclosures are clearly expressed.
   iv. *Accuracy and valuation*—financial and other information are disclosed fairly and at appropriate amounts.

Audit documentation: The record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached (terms such as "working papers" or "workpapers" are also sometimes used).

Audit evidence: Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.

> *Appropriateness (of audit evidence):* The measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based.
>
> *Sufficiency (of audit evidence):* The measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence.

Audit file: One or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement.

Audit risk: The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

Audit sampling (sampling): The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

Business risk: A risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity's ability to achieve its objectives and execute its strategies, or from the setting of inappropriate objectives and strategies.

Detection risk: The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

Emphasis of Matter paragraph: A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements.

Engagement partner- The partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

Engagement team: All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform procedures on the engagement. This excludes external experts engaged by the firm or a network firm.

Exception: A response that indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party.

Experienced auditor: An individual (whether internal or external to the firm) who has practical audit experience, and a reasonable understanding of:

a. Audit processes;
b. Auditing standards and applicable legal and regulatory requirements;
c. The business environment in which the entity operates; and
d. Auditing and financial reporting issues relevant to the entity's industry.

External confirmations: Audit evidence obtained as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.

Estimation uncertainty: The susceptibility of an accounting estimate and related disclosures to an inherent lack of precision in its measurement.

Financial statement level risk: Risks of material misstatement at the financial statement level refer to risks that relate pervasively to the financial statements as a whole and potentially affect many assertions. Risks of this nature are not necessarily risks identifiable with specific assertions at the class of transactions, account balance, or disclosure level. Rather, they represent circumstances that may increase the risks of material misstatement at the assertion level, for example, through management override of internal control. Financial statement level risks may be especially relevant to the auditor's consideration of the risks of material misstatement arising from fraud.

Fraud: An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

Internal control: The process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. The term "controls" refers to any aspects of one or more of the components of internal control.

Management: The person(s) with executive responsibility for the conduct of the entity's operations.

Management's expert: An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.

Management bias: A lack of neutrality by management in the preparation of information.

Misstatement: A difference between the amount, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud. To assist the auditor in evaluating the effect of misstatements accumulated during the audit and in communicating misstatements to management and those charged with governance, it may be useful to distinguish between factual misstatements, judgmental misstatements and projected misstatements.

Factual misstatements: are misstatements about which there is no doubt.

Judgmental misstatements are differences arising from the judgments of management concerning accounting estimates that the auditor considers unreasonable, or the selection or application of accounting policies that the auditor considers inappropriate.

Projected misstatements are the auditor's best estimate of misstatements in populations, involving the projection of misstatements identified in audit samples to the entire populations from which the samples were drawn.

Modified opinion: A qualified opinion, an adverse opinion or a disclaimer of opinion.

Non-compliance: Acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees. Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

Opening balances: Those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

Other matter paragraph : A paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

Pervasive: A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence. Pervasive effects on the financial statements are those that, in the auditor's judgment:

a) Are not confined to specific elements, accounts or items of the financial statements;
b) If so confined, represent or could represent a substantial proportion of the financial statements; or
c) In relation to disclosures, are fundamental to users' understanding of the financial statements.

Population: The entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions.

Preconditions for an audit: The use by management of an acceptable financial reporting framework in the preparation of the financial statements and the agreement of management and, where appropriate, those charged with governance to the premise on which an audit is conducted.

Professional judgment: The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

Professional skepticism: An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of evidence.

Reasonable assurance: A high, but not absolute, level of assurance.

Related party: A party that is either:

a) A related party as defined in the applicable financial reporting framework; or
b) Where the applicable financial reporting framework establishes minimal or no related party requirements:
    i. A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;
    ii. Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
    iii. Another entity that is under common control with the reporting entity through having:
        a. Common controlling ownership;
        b. Owners who are close family members; or
        c. Common key management.

However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another.

Risk assessment procedures: The audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.

Risk of material misstatement: The risk that the financial statements are materially misstated prior to audit. This consists of two components, described as follows at the assertion level:

Inherent risk: The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

Control risk: The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal control.

Sampling unit: The individual items constituting a population.

Significant risk: An identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration.

Subsequent events: Events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.

Substantive procedure: An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise Tests of details (of classes of transactions, account balances, and disclosures); and Substantive analytical procedures.

Tests of controls: An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level.

Those charged with governance: The person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Uncorrected misstatements: Misstatements that the auditor has accumulated during the audit and that have not been corrected.

Unmodified opinion: The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Written representation: A written statement by management provided to the auditor to confirm certain matters or to support other audit evidence. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records.