Naming:

I remember the section 105 special consideration on auditing standards, auditing of small entities. As you mentioned the main feature of these entities is not size. The main feature is how these entities are directed by management and how they operate and conduct their activities. So, as the term small entities was not appropriate the term “less complex” does not define these entities.

WHAT IS A LESS COMPLEX ENTITY?

I believe the definition of less complex entities well categorized in 2 parts but:

Part A: Concentration of ownership and management in a small number of individuals

I believe reference to users of the financial statements of these entities is necessary. As you know, in such entities the users of their financial statements are few users and accordingly the audit risk will be low. These entities often are not listed companies and have not a wide range of users. This feature should be added to this section. The concentration of ownership means these entities’ stocks are not transacted and accordingly there are no potential investors as users.

Part B: One or more of the following

- Straight forward or uncomplicated transactions
  
  It needs more explanation. Is it relating to monetary measurement process of transactions? Is it relating to need for estimation? It is better to say Straight forward or uncomplicated accounting transactions.

- Simple record keeping
  
  It needs more explanation. Is it relating to accounting treatments? Electronic commerce, start-up business or only to their book keeping systems.

- Few lines of product and few products within business lines
  
  What does it mean? Few lines of products. For example, Coca Cola produces drinks in pet and glass bottle or can; it produces diet, classic and reduced calorie. Is it few lines of products?
  
  Few products within business lines relates to size and is not important at all. It is not important how many units the entity produces but it is important how the products have been sold. Are there a lot of customers or the entity sells its products to a sole customer?

- Few internal control
  
  It should be changed to few internal controls or high risk of overriding exist controls by management (in fact the owners).

  - Few levels of management with responsibility for a broad range of controls.
  
  - Few personnel, many having a wide range of duties.
It should be change to few **key personnel** because it means the personnel that are in decision making position or personnel that have controlling duties. We do not mean production workers. In fact, it means few personnel in key areas of activities such as supervision or controlling the operation.

**Conclusion about the first issue:**

Before deciding about future action, we should give a comprehensive definition about less complex entities.

**Future actions**

As many other auditors I believe auditing is auditing and we do not need to establish separate set of auditing standards. We need guidelines about the application of certain standards; especially the risk assessment.

Central point of the case is internal control. Because of their structure and the risk of overriding internal control, we could not rely on internal control and this issue directs us toward changing our approach in auditing. Using substantive procedures including analytical procedures which are so important in case of Less Complex Entities.

Ali Sarehraz

Certified Public Accountant