



Subject: Agenda for the 104th meeting of the AUASB
Venue: ASIC offices, Level 5, 100 Market Street Sydney
Time: Monday 29 October 2018, 9.30am – 12.30pm

* NB: Agenda items 1 is a closed session.

Time	Agenda Item No.
9.30am	1. Preliminary Session* 1.1 Welcome and Introduction (verbal only) 1.2 AUASB Declarations of Interest 1.3 Update from the AUASB Chair (verbal only) 1.4 September IAASB meeting update
10:00am	2. ED ASA 315 Identifying and Assessing the Risks of Material Misstatements
11:00am	Break
11:15am	ED ASA 315 Identifying and Assessing the Risks of Material Misstatements (Continued)
12:00pm	3. ED ASA 540 Auditing Accounting Estimates and Related Disclosures
12:30pm	4. Close



AUASB Board Meeting Summary Paper

AGENDA ITEM NO. 2.1

Meeting Date: 29 October 2018

Subject: ED ASA 315 *Identifying and Assessing the Risks of Material Misstatement*

Date Prepared: 24 October 2018

☒ **Action Required**

☐ **For Information Purposes Only**

Agenda Item Objectives

1. **To consider responses and disposition of responses received** (Agenda Item 2.3) on Exposure Draft 01/18 Proposed Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* (ED 01/18) and Exposure Draft 02/18 Proposed Auditing Standard 2018-1 *Amendments to Australian Auditing Standards* (ED 02/18); and
2. **Consider and provide input** into the AUASB response to the IAASB on the IAASB's ED ISA 315 (Agenda Item 2.2).

Background

1. Exposure drafts ED 01/18 and ED 02/18 were issued on 7 August 2018 for a 70 day exposure period that ended 15 October 2018. The ED comprised an explanatory memorandum supporting a revised ASA 315 and an amending standard dealing with conforming amendments.
2. The AUASB received submissions from 7 stakeholders.

Considerations

Submissions Received

The AUASB technical group (ATG) received 7 formal submissions in relation to ED ASA 315. The disposition of all comments received is included as Agenda Item 2.3.

Feedback from Roundtables

The ATG held roundtables in Perth, Hobart, Canberra, Brisbane, Sydney and Melbourne in September and October 2018 where ED ASA 315 was discussed in detail and questions on exposure considered by stakeholders.

Stakeholder feedback was collated, summarised and considered by the ATG as part of the disposition of comments and draft submission to the IAASB.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

Approach to drafting submission

The AUASB received very detailed feedback on ED 315, and at times inconsistent feedback between stakeholders. The AUASB Technical Group (ATG) have considered all submissions and the feedback from the roundtables, and where there is consistent matters raised, these are in the draft submission for the AUASB's consideration. Where a matter has been raised by one stakeholder only, these have not been included this in the submission. The AUASB Comments and Proposed Disposition Paper details the points which are and are not in the draft submission for the AUASB's consideration.

Other National Standard Setters

NZAuASB

The ATG have reviewed and considered the NZAuASB draft submission on the IAASB Exposure Draft. There were no matters raised in the NZAuASB draft submission that have not been considered by the ATG.

“Compelling Reasons” Assessment

Based on the ATG's assessment of submissions received and feedback from the roundtables the AUASB technical group have not at this stage identified any compelling reasons, in accordance with the [Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board \(IAASB\) and Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board \(NZAuASB\) \(August 2014\)](#), that would need to be made to modify IAASB proposed standard.

Material Presented

2.1	AUASB Board Meeting Summary Paper - ED ASA 315 Identifying and Assessing the Risks of Material Misstatements
2.2	Draft AUASB Submission
2.3	AUASB Comments Received and Proposed Disposition Paper
2.3.1	Comment letter from Deloitte
2.3.2	Comment letter from Respondent 2 (Board Only)
2.3.3	Comment letter from KPMG
2.3.4	Comment letter from UNSW
2.3.5	Comment letter from ACAG
2.3.6	Comment letter from IIA
2.3.7	Comment letter from Respondent 7 (Board Only)
2.4	ED 315 Roundtables - Summary of Feedback



Australian Government

Auditing and Assurance Standards Board

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Melbourne VIC 3000 Australia
PO Box 204, Collins Street West
Melbourne VIC 8007

2 November 2018

Mr Dan Montgomery
Technical Director
International Auditing and Assurance Standards Board
International Federation of Accountants
529 5th Avenue, 6th Floor
New York, New York 10017 USA

Dear Dan,

**AUASB Submission on the IAASB's Proposed International Standard on Auditing ISA 315
(Revised) *Identifying and Assessing the Risks of Material Misstatement***

The Australian Auditing and Assurance Standards Board (AUASB) is pleased to comment on the IAASB's Proposed International Standard on Auditing ISA 315 (Revised) *Identifying and Assessing the Risks of Material Misstatement* (ED 315), and conforming amendments to other ISAs.

In formulating its response, the AUASB has sought input from its stakeholders in three principal ways. The first was from hosting a series of roundtable meetings with stakeholders in six of the large Australian cities - stakeholders representing a broad range of backgrounds including assurance providers from small, medium and large audit firms, professional accounting bodies, directors and preparers of financial statements. The second was through an open invitation to provide comments on the AUASB issued equivalent exposure drafts; and the third was by way of formal discussions by the AUASB members at recent AUASB meetings.

Overall the AUASB is supportive of the IAASB's proposed revisions to ISA 315. The AUASB considers these revisions will achieve the objective of establishing more robust requirements and appropriately detailed guidance to drive auditors to perform consistent and effective risk assessment. However the AUASB raises the following key point for the IAASB's consideration.

Whilst we support the IAASB's intention to ensure ED 315 can be applied to the audits of small, non-complex entities to large, complex, multinational entities, its complexity and length makes scalability challenging. The AUASB considers that the definitions of relevant assertions and significant risks further impact the scalability of ED 315. The AUASB recommends that the IAASB further enhance ED 315 to improve scalability and that non-authoritative guidance in the form of frequent asked questions and examples are developed to assist with implementation. Please refer to question 2 of our submission for further our suggestions on how to achieve this.

Please refer to our detailed comments in Appendix 1.

Should you have any queries regarding this submission, please do not hesitate to contact me or Matthew Zappulla at mzappulla@auasb.gov.au.

Yours sincerely,

Professor Roger Simnett AO
Chair

Draft

1. Has ED 315 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risks of material misstatement? In particular:

(a) Do the proposed changes help with the understandability of the risk identification and assessment process?

Yes. The AUASB considers that ED 315 has provided significant clarification about the risk identification and assessment process and has been appropriately restructured, clarified and modernised. We support the principles-based approach in ED 315 whilst providing a more granular and robust process which we believe promotes understandability and aids in identifying and assessing the risks of misstatement.

Whilst we understand that risk identification and assessment is a complex and iterative process with many steps occurring concurrently, ED 315 is complex and its length may be a barrier to its understandability, and scalability. The IAASB should also consider the following to assist with the overall understandability of ED 315:

- Whether some content in the application material may be included in other non-authoritative guidance. Refer to question 2 for further comments.
- Clearer linkage between the “understanding” obtained regarding each of the components of the entity’s system of internal control and how this is applied to identify and assess the risks of material misstatement. Refer to question 5 for further comments.
- Further clarification on how inherent risk and control risk interact and combine when assessing the risks of material misstatement. Refer question 6a for further comments.

(a) (continued) Are the flowcharts, prepared by the IAASB, helpful in understanding the flow of the standard (i.e., how the requirements interact and how they are iterative in nature)? If yes, should they be included in the final Standard?

The flowcharts are helpful in understanding ED 315. The AUASB supports the flowcharts being included as appendices to the final standard. In the AUASB’s view the flowcharts could be further enhanced to clearly present and emphasise what is inherently an iterative process in a more straight forward manner.

(b) Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6–28 of the IAASB’s Explanatory Memorandum.

The AUASB agrees that ED 315 provides a more granular and robust process for the identification and assessment of the risks of material misstatement. We believe this more granular and robust processes will assist with consistency of the risk identification and assessment process. We also agree that any public interest issues are well addressed.

(c) Are the new introductory paragraphs helpful?

The AUASB considers the introductory paragraphs greatly assist with the understandability of the risk identification and assessment process and explain important concepts, however the AUASB believe that to avoid confusion it would be useful to describe the status of these paragraphs (ie. are they authoritative?) We also consider that the introductory paragraphs should be enhanced as follows:

- Paragraph 4 should state more clearly that the initial identification of risk of material misstatement is based on the inherent risk assessment only.
- Describe the “spectrum of inherent risk” in more detail or refer to the application material.
- Provide an overview of the identification and assessment of the risk of material misstatement at the financial statement level.

2. Are the requirements and application material of ED 315 sufficiently scalable, including the ability to apply ED 01/18 to the audits of entities with a wide range of sizes, complexities and circumstances?

We support the IAASB's intention to ensure ED 315 can be applied to the audits of small, non-complex entities to large, complex, multinational entities. The AUASB considers that scalability could be enhanced by the following:

- The length of ED 315 is a barrier to understanding the standard, and in particular for audits of smaller and less complex entities. We recommend that the IAASB consider how the application material in ED 315 can be reduced. Refer to question 1a for further comments.
- ED 315 uses the term smaller and less complex entities. However complexity is the key driver in scalability when performing risk assessment. Smaller entities may be complex, and conversely larger entities may be less complex. We recommend the terminology used in ED 315 should refer to "less complex entities" which will allow this guidance to be used in audits regardless of size. We note that "less complex entities" is the terminology used in the IAASB's future discussion paper on this topic.
- The use of the term "more than remote" in the definition of Relevant Assertion will increase the audit work effort over low risk balances as most assertions will meet this test, and therefore will result in more significant classes of transactions, account balances, or disclosures. Refer to question 6d for further comments.
- Provide more guidance and examples on how to effectively scale the work effort to less complex entities such as:
 - An example of how to perform risk identification and assessment for a less complex entity where a mainly substantive audit approach will be adopted to be included in the application material.
 - Examples of how the system of internal control may be less detailed and formalised.
 - How to gather the understanding of the IT environment / identification of risks arising from IT and identification and evaluation of GITCs.

3. Do stakeholders agree with the approach taken to enhancing ED 01/18 in relation to automated tools and techniques, including data analytics, through the use of examples to illustrate how these are used in an audit (see Appendix 1 of the IAASB's Explanatory Memorandum for references to the relevant paragraphs in ED 01/18)? Are there other areas within ED 315 where further guidance is needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?

Yes, the AUASB agrees with the approach taken of using examples to illustrate how automated tools and techniques may be used in risk assessment. Our stakeholders support the explicit reference to and including of examples of automated tools and techniques in ED 315. We are also supportive of avoiding terminology that may become outdated quickly.

We consider that ED 315 should also address:

- How automated tools and techniques may be used for risk assessment, and how they meet or impact the requirements of ED 315. This is to avoid automated tools and techniques being applied in addition to the current requirements of the standard.
- What are the requirements in relation to understanding and/or obtaining evidence over the reliability of underlying data (information produced by the entity) used within automated tools and techniques that is used for risk assessment (including the nature, timing and extent of testing).
- Risk factors relating to the use of big data and automated analytics technology.

In addition paragraph 54 and A15, A18 and A32 – 33 could be enhanced by:

- Risk considerations or documentation requirements specific to the use of predictive analytics or analytic tools that incorporate machine learning or artificial intelligence (AI) by both entities and auditors, particularly the nature of what is considered “Audit Evidence”.
- Documentation requirements for analytic procedures to allow for re-performance where machine learning is used by an entity and/or the auditor.
- Consideration of the requirements in relation to General Information Technology Controls testing and database control assurance required when using automated tools as part of risk assessment.
- Documentation requirements on the appropriateness and reliability of external data sets (being data sets external to the entity’s sphere of control).
- Guidance on how audit analytics and automated tools can be used to assess qualitative inherent risks factors described in section A5.

4. Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk identification and assessment process? Do you support the proposed change for the auditor to obtain ‘sufficient appropriate audit evidence’¹ through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional scepticism?

The AUASB agrees that the application of professional scepticism is reinforced throughout the risk identification and assessment process in ED 315. Specifically we agree with the principles-based approach and reference to the concept of professional scepticism in the introductory paragraphs, rather than prescriptive requirements.

Based on academic research we recommend the following enhancements to ED 315 to encourage higher levels of professional scepticism:

- Paragraph 22 - the engagement partner is to use professional judgment to decide the format of instructions provided, and who will participate, when conducting the discussion.
- Paragraph A45 - be expanded to note that the engagement partner should be cognisant, when communicating with those not included in the discussion, that what they communicate, and how they communicate, might lead to auditor bias which can, depending on the circumstances, both positively and negatively impact the level of professional scepticism being exercised.
- Paragraph A19 include reference to broad sources of information (that may include but not limited to the points noted) so as to avoid consciously and/or subconsciously narrowing the breadth of information search.
- Paragraph A42 include the other benefits of the engagement team discussion including helping auditors to be open to new information, and different interpretations of the information, and to limit the possibility of prematurely forming a belief.

The AUASB is supportive of the principle of obtaining an appropriate base of evidence for risk assessment. However some stakeholders have raised concerns about using the term “sufficient appropriate audit evidence” in paragraph 17, as this term is associated with drawing conclusions on the evidence collected on the financial statements as a whole and not during the risk identification and assessment phase. We have also noted that using this term in ED 315 is inconsistent with the definition of audit evidence in ISA 200. We believe the IAASB need to consider if paragraph 17 is appropriate, and the impact this has on ISA 200. We also recommend that further guidance is required to explain how this is to be interpreted.

5. Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks or material misstatement? Specifically:

¹ See paragraph 27 of the IAASB’s Explanatory Memorandum and paragraph 17 of ED 01/18

- (a) **Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?**

The AUASB considers that ED 315 provides greater clarity in relation to what is required when obtaining an understanding of each component of the entity’s system of internal control and how this informs the risk identification and assessment process. Additionally the flowcharts and the updated definitions provide greater clarity. However in the AUASB’s view the following changes are required to enhance clarity and flexibility:

paragraph 35 (a) (ii) “Information about significant events and conditions...”

paragraph 39 (a) “... procedures alone ~~do~~ may not provide sufficient...”

paragraph 40 (d) “... substantive procedures alone ~~do~~ may not provide sufficient ...”

- (b) **Have the requirements related to the auditor’s identification of controls relevant to the audit² been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?**

The AUASB considers that ED 315 paragraph 39 (and A166 and A167) provides clarity on the identification of controls relevant to the audit, including clarifying that most controls that are relevant to the audit will be direct controls in the Information System and Communication and Control Activities components. We recommend that the IAASB clarify the intention of 39(e), or consider removing this, as the controls relevant to the audit are captured appropriately in the preceding elements of this paragraph.

Para A166 and A167 provide appropriate clarity that based on their judgement of the complexity and size of an entity conclude that the only relevant controls are those over journal entries if they do not plan to rely on any of the other controls.

- (c) **Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor’s understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor’s consideration of the effects of the entity’s use of IT on the identification and assessment of the risks of material misstatement?**

The AUASB supports the introduction of the new IT-related concepts and definitions. We agree that the enhancements contained in ED 315 assist greatly in understanding the impact of the IT environment and how to identify IT controls including general IT controls which are relevant to the audit.

We consider that ED 315 could be enhanced by including the risk factors relating to current and evolving technology which connect to organizational networks, such as infrastructure / software as a service solutions, wireless networks, blockchain, and other technology devices that connect to organisational networks.

6. Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:

- (a) **Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments’?**

The AUASB supports the separate assessments of inherent and control risk at the assertion level and consider that the related requirements and guidance are appropriate. We are also

² See ED 01/18, paragraphs 39-40 and paragraphs 37-40 of the IAASB’s Explanatory Memorandum

supportive of the explicit requirement to assess control risk at maximum if the operating effectiveness of controls are not being tested.

We recommend that the IAASB provide clarity on how this separate assessment is done through the following changes:

- Paragraph 45 should reflect that it applies to the Inherent Risk component of risk of material misstatement not the combined risk of material misstatement (after combination of control risk).
- Describe how these assessments are combined to determine the risk of material misstatement.
- Providing detail on how to assess control risk. ED 315 only refers to the concepts of maximum, or less than maximum.

(b) Do you support the introduction of the concepts and definitions of ‘inherent risk factors’ to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor’s risk assessment process?

The AUASB supports the concepts and definitions of inherent risk factors and how they are used to identify risks of material misstatement and assess inherent risk. We consider this will result in more robust risk identification and assessment as will help auditors focus on the characteristics that affect susceptibility to misstatement.

However as “Inherent Risk Factors” (16(f) and A6) include the quantitative significance of a class of transactions, account balance or disclosure in relation to performance materiality, it would appear that all material items would have a risk of material misstatement and be identified as significant. We question if this is the intended consequence and do not agree that all classes of transactions, account balances or disclosures should be considered “significant” based on quantitative factors along which is how 16(f) and A6 may be interpreted. This will also impact whether a stand back requirement is required in both ED 315 and ISA 330 (refer question 8 for further comments).

(c) In your view, will the introduction of the ‘spectrum of inherent risk’ (and the related concepts of assessing the likelihood of occurrence, and magnitude, of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?

The AUASB is supportive of the introduction of the “spectrum of inherent risk” and auditors considering how inherent risk factors individually or in combination increase inherent risk to varying degrees. The consideration of inherent risk factors and the concept of the spectrum of inherent risk help auditors consider the susceptibility to misstatement and the risks, when assessing inherent risk.

However we believe more guidance is required to assist auditors to determine at which point on the spectrum a risk resides, and where on the scale of likelihood and magnitude would result in a significant risk i.e. would a low likelihood and high magnitude result in a significant risk. Refer 6(e) for further comments on the definition of significant risk.

(d) Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e., an assertion is relevant when there is a reasonable possibility of occurrence of a

misstatement that is material with respect to that assertion),³ and how they assist the auditor in identifying where risks of material misstatement exist?

We are supportive of the proposed definitions of significant classes of transactions, account balances and disclosures. However we are not supportive of the proposed definition of relevant assertions. A relevant assertion is an assertion where there is a “reasonable possibility” of occurrence of a misstatement, which is defined as when the likelihood of a material misstatement is “more than remote”. No guidance is provided on how to assess this. Our stakeholders strongly consider that “more than remote” is different to “reasonable possibility”, and are concerned that this will create issues for scalability, as many assertions may meet this test, and therefore result in more significant significant classes of transactions, account balances, or disclosures being identified. We do not agree this is the desired outcome. More guidance is required.

The AUASB is aware of research that supports that these terms are interpreted differently by auditors. The AUASB can share this research with the IAASB if requested.

(e) Do you support the revised definition,⁴ and related material, on the determination of ‘significant risks’? What are your views on the matters presented in paragraph 57 of the IAASB’s Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?

We support the definition of significant risk being aligned to the nature of the risk and the susceptibility to fraud or error, and not the auditor’s response to a risk as it is in extant ISA 315. To provide further clarity on this definition, the AUASB recommends:

- The definition of significant risk be amended to those “at the upper end of the spectrum of inherent risk” and not “close to the upper end of the spectrum of inherent risk”.
- Additionally as stated above in question 6(c) additional guidance is required in how to assess where on the spectrum a risk resides, and where a significant risk resides on the scale of likelihood and magnitude.
- Paragraph A10 be enhanced to explain how the “spectrum of inherent risk” works in identifying significant risks. A10 focuses more on the implications for the audit, and not on the identification of inherent risk.

In relation to the definition of significant risk and the matters presented in paragraph 57 of the IAASB’s Explanatory Memorandum, stakeholders had differing views as to whether the term high likelihood of occurrence OR the magnitude of potential misstatement, or high likelihood of occurrence AND the magnitude of the potential misstatement, is the most appropriate. The IAASB’s Explanatory Memorandum details that the IAASB’s view is that for risks low in likelihood, but for which the magnitude could be very high if it occurred, it wasn’t appropriate to explicitly exclude these from the auditor’s determination of significant risks. The AUASB considers, risks with a very low likelihood, but high magnitude should not be automatically significant risks, and therefore the definition should be changed so auditors consider likelihood and magnitude in combination when determining significant risk.

7. Do you support the additional guidance in relation to the auditor’s assessment of risks of material misstatement at the financial statement level,⁵ including the determination about how, and the degree to which, such risks may affect the assessment of risks at the assertion level?

Yes the AUASB agrees that the additional guidance in relation to financial statement level risks explains how these are assessed at the assertion level. However we consider that auditors find this difficult in practice and more guidance or examples could be provided. We note that Appendix 2

³ See footnote 26 of the IAASB’s Explanatory Memorandum.

⁴ Paragraphs 16(k) and A10, and A229-A231 of ED 01/18.

⁵ Paragraphs 47 and A215–A220 of ED 01/18.

only includes examples of risks of material misstatement at the assertion level and should also include at least one example of risk of material misstatement at the financial statement level, and how this may affect the assessment of risks at the assertion level.

- 8. What are your views about the proposed stand-back requirement in paragraph 52 of ED 01/18 and the proposed revisions made to paragraph 18 of ISA 330 and its supporting application material? Should either or both requirements be retained? Why or why not?**

The AUASB supports the concept of a stand back requirement in ED 315. Our stakeholders had mixed views as to whether the stand back requirement is better placed in ED 315 or ISA 330, however there was consensus that it is not required in both. On balance the majority of our stakeholders prefer a stand back requirement in ED 315 as this will result in a more robust risk assessment process, which is important in improving overall audit quality. Therefore if a class of transactions, account balances or disclosures has not been assessed as significant as there is no risk of material misstatement then ISA 330 paragraph (18) should not be required.

However as “Inherent Risk Factors” (16(f) and A6) include the quantitative significance of a class of transaction, account balance or disclosure in relation to performance materiality, it would appear that all material items would be considered significant. We question if this is the intended consequence and do not agree that all classes of transactions, account balances or disclosures should be considered significant based on quantitative factors along which is how 16(f) and A6 may be interpreted. Refer to question 6(b).

Conforming and consequential amendments

- 9. With respect to the proposed conforming and consequential amendments to:**

- (a) ISA 200 (including Appendix 2), ISA 240 and ED 03/18, are these appropriate to reflect the corresponding changes made in proposed ISA 315?**

Refer to question 4. Using the term “sufficient appropriate audit evidence” in paragraph 17 is inconsistent with the definition of audit evidence in ISA 200. We believe the IAASB need to consider if paragraph 17 is appropriate, and the impact this has on ISA 200.

- (b) ISA 330, are the changes appropriate in light of the enhancements that have been made in proposed ISA 315, in particular as a consequence of the introduction of the concept of general IT controls relevant to the audit?**

No matters noted.

- (c) The other ISAs as presented in Appendix 1, are these appropriate and complete?**

A stakeholder requested that the IAASB also consider reviewing whether confirming amendments are necessary for ISA 402 and ISA 600.

- 10. Do you support the proposed revisions to paragraph 18 of ISA 330 to apply to classes of transactions, account balances or disclosures that are ‘quantitatively or qualitatively material’ to align with the scope of the proposed stand-back in proposed ISA 315?**

The AUASB supports the removal of ISA 300 paragraph 18. Refer to question 8.

- 11. Effective date: the IAASB have proposed that the standard will be effective for financial reporting periods commencing no or after 15 December 2020, which is anticipated to be approximately 18 months after approval of the final ISA. Do you think this is a sufficient period to support effective implementation of the new standard?**

Effective date is appropriate.

Other matters raised by stakeholders

We also highlight the following for the IAASB's consideration:

Documentation:

Stakeholders raised overall concerns about the level of documentation that may be required to evidence compliance with ED 315. To assist auditors the AUASB recommend that the IAASB issue non-authoritative guidance outlining the documentation requirements specific for a less complex entity.

Public sector considerations

We received feedback from public sector auditor representatives that the considerations specific to the public sector do not articulate their requirements to consider the risks of probity and propriety and the need to comply with legislated financial accountability frameworks (ED 315 - A36).

Draft



AUASB Comments Received and Proposed Disposition Paper

AGENDA ITEM NO. 2.3

Meeting Date: 29 October 2018

Subject: Exposure Draft 01/18 Proposed Auditing Standard ASA 315 Identifying and Assessing the Risks of Material Misstatement

Date Prepared: 24 October 2018

Document Type: Exposure Draft

Document Number: ED 01/18 & 02/18

Proposed Type & No: ASA 315

Proposed Title: ASA 315 Identifying and Assessing the Risks of Material Misstatement

	Page Number
EXHIBIT 1: Comments on specific questions ED 01/18	7
EXHIBIT 2: Comments on specific questions ED 02/18	61
EXHIBIT 3: Other comments on ED 01/18 & ED 02/18	71

Objective of paper:

The objective of this paper is to list all responses to [ED 01/18](#) and [ED 02/18](#), grouping responses by question. Each comment has been cross-referenced to the relevant submission in the column **Ref Page No.** The **ATG commentary** column includes the ATG's response to each comment and whether the point has been carried forward to the AUASB draft submission.

A list of respondents has been provided on page 2. Note that two of the respondents requested submissions to be treated as confidential and have been de-identified for the purposes of the disposition paper. A full list of questions asked in ED 01/18 and ED 02/18 with page references have been included on pages 3-6.

This document contains preliminary views and/or AUASB Technical Group recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.

LISTING OF RESPONDENTS

Short Form Name	Name	Date Received
Deloitte	Deloitte Touche Tohmatsu	11 October 2018
R2	Respondent 2 (confidential submission)	15 October 2018
KPMG	KPMG	16 October 2018
UNSW	University of New South Wales	15 October 2018
ACAG	The Australasian Council of Auditors-General	15 October 2018
IIA	The Institute of Internal Auditors	5 September 2018
R7	Respondent 7 (confidential submission)	16 October 2018

LISTING OF QUESTIONS

ED 01/18 *Proposed Auditing Standard ASA 315 Identifying and Assessing the Risks of Material Misstatement*

	Page #
Question 1 – Has ED 01/18 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risks of material misstatement. In particular:	
Qn. 1(a) – Do the proposed changes help with the understandability of the risk identification and assessment process?	7
Qn. 1(b) – Are the flowcharts helpful in understanding the flow of the standard (i.e., how the requirements interact and how they are iterative in nature)? If yes, should they be included in the final ISA 315?	11
Qn. 1(c) – Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6–28 of the IAASB’s Explanatory Memorandum?	12
Qn. 1(d) – Are the new introductory paragraphs helpful?	14
Question 2 – Are the requirements and application material of ED 01/18 sufficiently scalable, including the ability to apply ED 01/18 to the audits of entities with a wide range of sizes, complexities and circumstances?	15
Question 3 – Do respondents agree with the approach taken to enhancing ED 01/18 in relation to automated tools and techniques, including data analytics, through the use of examples to illustrate how these are used in an audit (see Appendix 1 of the IAASB’s Explanatory Memorandum for references to the relevant paragraphs in ED 01/18)? Are there other areas within ED 01/18 where further guidance is needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?	18
Question 4 – Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk identification and assessment process? Do you support the proposed change for the auditor to obtain ‘sufficient appropriate audit evidence’¹ through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional scepticism?	20
Question 5 – Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control² assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks or material misstatement? Specifically:	
Qn. 5(a) – Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?	25
Qn. 5(b) – Have the requirements related to the auditor’s identification of controls relevant to the audit been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?	29

Qn. 5(c) – Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor’s understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor’s consideration of the effects of the entity’s use of IT on the identification and assessment of the risks of material misstatement?	31
Question 6 – Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:	
Qn. 6(a) – Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments’?	33
Qn. 6(b) – Do you support the introduction of the concepts and definitions of ‘inherent risk factors’ to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor’s risk assessment process?	36
Qn. 6(c) – In your view, will the introduction of the ‘spectrum of inherent risk’ (and the related concepts of assessing the likelihood of occurrence, and magnitude, of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?	37
Qn. 6(d) – Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e., an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion), and how they assist the auditor in identifying where risks of material misstatement exist?	39
Qn. 6(e) – Do you support the revised definition, and related material, on the determination of ‘significant risks’? What are your views on the matters presented in paragraph 57 of the IAASB’s Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?	43
Question 7 – Do you support the additional guidance in relation to the auditor’s assessment of risks of material misstatement at the financial statement level, including the determination about how, and the degree to which, such risks may affect the assessment of risks at the assertion level?	45
Question 8 – What are your views about the proposed stand-back requirement in paragraph 52 of ED 01/18 and the proposed revisions made to paragraph 18 of ASA 330 and its supporting application material? Should either or both requirements be retained? Why or why not?	47
Question 9 – Effective Date: the IAASB have proposed that the standard will be effective for financial reporting periods commencing on or after 15 December 2020, which is anticipated to be approximately 18 months after approval of the final ISA 315. Do you think this is sufficient period to support effective implementation of the new standard?	50
Question 10 – Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?	52
Question 11 – Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?	53
Question 12 – Whether there are any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?	54

Question 13 – What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand: (a) Where those costs are likely to occur; (b) The estimated extent of costs, in percentage terms (relative to audit fee); and (c) Whether expected costs outweigh the benefits to the users of audit services?	57
Question 14 – What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 315 (specific questions/examples would be helpful)?	59
Question 15 – Are there any other significant public interest matters that stakeholders wish to raise?	60

ED 02/18 Proposed Auditing Standard ASA 2018-1 Amendments to Australian Auditing Standards (Conforming and consequential amendments arising from the proposed revisions to ASA 315)

	Page #
Question 1 – With respect to the proposed conforming and consequential amendments to::	
Qn. 1(a) – ASA 200 (including Appendix 2), ASA 240 and ED 03/18, are these appropriate to reflect the corresponding changes made in proposed ASA 315?	61
Qn. 1(b) – ASA 330, are the changes appropriate in light of the enhancements that have been made in proposed ASA 315, in particular as a consequence of the introduction of the concept of general IT controls relevant to the audit?	62
Qn. 1(c) – The other ASAs as presented in Appendix 1, are these appropriate and complete?	63
Question 2 – Do you support the proposed revisions to paragraph 18 of ASA 330 to apply to classes of transactions, account balances or disclosures that are ‘quantitatively or qualitatively material’ to align with the scope of the proposed stand-back in proposed ASA 315?	64
Question 3 – Effective Date: the IAASB have proposed that the standard will be effective for financial reporting periods commencing on or after 15 December 2020, which is anticipated to be approximately 18 months after approval of the final ISA 315. Do you think this is sufficient period to support effective implementation of the new standard?	65
Question 4 – Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?	66
Question 5 – Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?	67

Question 6 – Whether there are any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?	68
Question 7 – What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand: (d) Where those costs are likely to occur; (e) The estimated extent of costs, in percentage terms (relative to audit fee); and (f) Whether expected costs outweigh the benefits to the users of audit services?	69
Question 8 – Are there any other significant public interest matters that stakeholders wish to raise?	70

EXHIBIT 1: Comments on specific questions ED 01/18

Question 1 – Has ED 01/18 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risks of material misstatement. In particular:

Qn. 1(a) – Do the proposed changes help with the understandability of the risk identification and assessment process?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 2	Deloitte	<p>a) Overall we believe the changes to ED 01/18 are improvements to the previous version of the standard, however there does remain a number of areas that may cause misunderstanding or confusion (for example, the concept of a significant class of transactions, account balance or disclosure versus a material class of transactions, account balance or disclosure; inherent risk versus control risk and the consideration of controls when identifying and assessing risks of material misstatement), which need to be addressed prior to the revisions, promoting a robust risk identification and assessment process.</p> <p>b) The complexity and professional judgement required when identifying and assessing the risks of material misstatement, as well as the sheer volume of the standard also create potential application challenges relating to consistency and robustness.</p> <p>c) We believe the first point that needs to be made clear is the identification of a risk of material misstatement versus the assessment of a risk of material misstatement. The next point is in relation to differentiating between having an 'understanding of internal control' (as included in paragraph 4) when identifying risks of material misstatement versus assuming that the entity's controls are operating effectively and thus influencing whether a risk of material misstatement exists or not.</p> <p>d) Ultimately, the understanding of the internal control structure including the design and implementation of controls is appropriate and required when identifying and assessing risks of material misstatement, however auditors are unable to conclude that there is a remote risk (therefore not a risk of material misstatement) by assuming that one or more controls are operating effectively - this is what needs to be clearly communicated within the standard.</p>	<p>(a) This has not been raised by other respondents so has not been included in the AUASB submission;</p> <p>(b) Consistent with feedback received from other stakeholders. Included in AUASB Submission;</p> <p>(c) The view of the ATG is that this is clear within the standard, and has not been carried forward to the AUASB Submission;</p> <p>(d) Consistent with feedback received from other stakeholders. Included in AUASB Submission;</p> <p>(e) Consistent with feedback received from other stakeholders. Included in AUASB Submission; and</p> <p>(f) Consistent with feedback received from other stakeholders. Included in AUASB Submission.</p>

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>e) It is unclear how inherent risk and control risk interacts and combines together when it comes to assessing the risks of material misstatement.</p> <p>f) For instance, paragraph 5 states "For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk and control risk is required by this ASA." However no requirements or guidance is provided on how these separate assessments then combine together to form the overall assessment of the risk of material misstatement</p>	
2	Page 3	R2	We support the general principles of the revised standard and note its improvement on the extant ASA 315. However, we do detail below some concerns in response to the questions raised.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
3	Pages 5-6.	KPMG	<p>We are supportive of the overall direction of the proposed changes to ISA 315 and believe that these are helpful in addressing the public interest issues.</p> <p>In general, we believe that ED 01/18 has provided significant clarification regarding many aspects of the process for the identification and assessment of the risks of material misstatement, in comparison to the extant standard. In particular, the introductory paragraphs, the flowcharts and the increase in “signposts” or “milestones” help with the understandability of the standard, both in terms of the flow, the overall objectives, and how each part of the process supports the achievement of these objectives. In this regard, we recommend that the flowcharts are ultimately included as part of the standard.</p> <p>Nevertheless, this is a highly complex standard, with much of this complexity residing in the fact that an auditor executes the procedures required in an iterative, rather than a linear fashion, as described in the Explanatory Memorandum to the ED, as well as in the application material. Furthermore, as we describe in our overarching comments, many “steps” are in practice performed concurrently, and in doing so, implicit consideration is given by the auditor to the results or expected results relating to other aspects of the standard. This level of intricacy, which will vary depending on the engagement circumstances, is challenging to describe in the standard itself, and is also very difficult to capture clearly in flowcharts, which therefore summarise the written material but do not provide more meaningful insights as to its application.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>We also note in our overarching comments that the requirements are supported by lengthy and detailed application material, to a much greater extent than is the case for other ISAs. We believe that this compounds the difficulties in understanding the intended flow of the standard.</p> <p>We consider that the standard would particularly benefit from clearer linkage between the “understanding” obtained regarding each of the components of the entity’s system of internal control and how this is applied in fulfilling the requirements to identify and assess the risks of material misstatement at paragraph 45 onwards. Paragraph 17 describes this understanding as forming the basis for the risk identification and assessment. However, the application material, in particular A201 and A202, focuses more on the inter-relatedness of these aspects of the standard, e.g. that the auditor forms initial expectations and then confirms or updates these, or that information gathered in performing the risk assessment procedures to obtain the understanding is used as audit evidence to support the risk assessment. Paragraph A208 states that the identification of risks of material misstatement at the assertion level is performed before consideration of any controls, which seems to contradict this linkage insofar as risks of material misstatement at the assertion level are concerned.</p> <p>We suggest that the IAASB consider including further enhancements to the ED to avoid confusion and inconsistency in application of the standard, such as, at a minimum, increased cross-referencing between relevant areas of the standard, in particular in respect of steps that may be performed concurrently. We also recommend that the IAASB may wish to explore alternative or additional flowcharts, or a tabular presentation, to provide a more meaningful summary of the simultaneous nature of the performance of certain key requirements, as well as to illustrate where implicit consideration is made of the results of other steps, and where initial expectations are formed, and then refined, during the performance of certain procedures.</p>	
4	N/A	UNSW	No response provided.	N/A
5	Page 2	ACAG	<p>ACAG agrees that there is generally an improvement in understandability and description of risk.</p> <p>Service entity use is rising and should be considered when obtaining an understanding of the entity’s system of internal control. ACAG considers that</p>	Include in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			additional considerations in this standard or ASA 402 <i>Audit Considerations Relating to an Entity Using a Service Organisation</i> would be beneficial.	
6	N/A	IIA	No response provided.	N/A
7	Page 1	R7	Our initial discussions have not identified any serious issues with the ability of the requirements in the ED to be operationalised however, there are concerns with the length and complexity of the standard which may result in challenges for SMPs trying to incorporate it into their methodologies. We appreciate that risk identification and assessment is a complex and iterative process which is not easy to present in narrative form. Therefore we expect it would be well received if the IAASB incorporated the flowcharts or other diagrammatical representation into the body of the standard to simplify its presentation.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Qn. 1(b) – Are the flowcharts, prepared by the IAASB, helpful in understanding the flow of the standard (i.e., how the requirements interact and how they are iterative in nature)? If yes, should they be included in the final Standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 2.	Deloitte	<p>We understand that the flowcharts are aimed to add value, however we also acknowledge that due to the complexity and iterative nature of risk assessment, the flowcharts do require careful consideration and are not "quick reference guides". There are some challenges with the ordering and sequencing of certain steps (for example, relating to the identification of material but not significant classes of transactions, account balances and disclosures after identifying and assessing the significant classes of transactions, account balances and disclosures) within the flowcharts.</p> <p>If flowcharts are included in the final standard, it is important that they clearly present what is inherently an iterative process and where multiple steps are concurrently occurring.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
2	Page 3.	R2	The flowcharts are an excellent addition to the proposed ASA 315 and should be incorporated as appendices or guidance to the standard but not as mandatory elements of the standard. They enhance the understanding of the intent of the standard setters consistent with the inclusion of the introductory paragraphs to assist auditors in obtaining an overview of the standard. However, the flow charts should not be seen as a substitute for understanding the standard in its full form.	Consistent with feedback received from other stakeholders. Included in AUASB Submission
3	Page 5.	KPMG	In this regard, we recommend that the flowcharts are ultimately included as part of the standard.	Consistent with feedback received from other stakeholders. Included in AUASB Submission
4	N/A	UNSW	No response provided.	N/A
5	Page 2.	ACAG	ACAG supports flowcharts being included in the final standard. The flowcharts clarify both the logical flow of the standard and clearly describe the processes required of auditors to understand the control environment.	Consistent with feedback received from other stakeholders. Included in AUASB Submission
6	N/A	IIA	No response provided.	N/A
7	Page 1.	R7	We expect it would be well received if the IAASB incorporated the flowcharts or other diagrammatical representation into the body of the standard to simplify its presentation.	Consistent with feedback received from other stakeholders. Included in AUASB Submission

Qn. 1(c) – Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6–28 of the IAASB’s Explanatory Memorandum.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 2.	Deloitte	Yes, however we believe there are a number of inconsistencies and areas needing clarification relating to key concepts and terminology that need to be addressed. Refer to our response to question 1 (a) above, as well as Appendix 2.	Consistent with feedback received from other stakeholders. Included in AUASB Submission
2	Page 3.	R2	In principle the revisions provide more granular process and understanding of the intent of the standard setters around the requirements of the risk assessment process. There are however, some points of concern within the standard these are addressed further in the response. With respect to the increase in the robustness of the process, the standard in most instances clarified the extant standard where it was executed appropriately previously I do not believe the current standard will result in a more robust process for identifying risks, as it is clarification rather than changing of the process, however it will result in greater documentation requirements and costs in performing the audit.	Consistent with feedback received from other stakeholders. Some points included in AUASB Submission
3	Page 5.	KPMG	In general, we believe that ED 01/18 has provided significant clarification regarding many aspects of the process for the identification and assessment of the risks of material misstatement, in comparison to the extant standard. In particular, the introductory paragraphs, the flowcharts and the increase in “signposts” or “milestones” help with the understandability of the standard, both in terms of the flow, the overall objectives, and how each part of the process supports the achievement of these objectives.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Pages 2-3.	ACAG	<p>ACAG agrees that the revisions will promote a more robust risk assessment process. We are supportive of the clarification that when the operating effectiveness of controls are not tested the auditors shall assess controls risk at the maximum.</p> <p>The public interest issues are reasonably well addressed. ACAG makes the following comments in relation to specific aspects of the proposed requirements:</p> <ul style="list-style-type: none"> - The inherent risk factor of susceptibility to management bias is a helpful clarification and distinction to fraud risks, as are the broader statements regarding qualitative aspects. - The auditor’s use of data analytics tools in risk assessments is not well considered and ACAG makes further comment on this under question 3 below. 	Agree. Public interest points included in the AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<ul style="list-style-type: none"> - Considerations specific to the public sector do not articulate our requirements to consider the risks of probity and propriety and the need to comply with legislated financial accountability frameworks (A36). - Although paragraph A51 encourages the auditor to consider the responsibilities of those charged with governance for oversight of financial reporting, this paragraph does not address the need for an auditor to also consider the responsibilities of those charged with governance for the accuracy and relevance of the data used in business intelligence reporting. 	
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 1(d) – Are the new introductory paragraphs helpful?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 2.	Deloitte	<p>We consider the introductory paragraphs to be too detailed in the context of their purpose as an introduction. As a consequence of this detail they:</p> <ul style="list-style-type: none"> - attempt to introduce multiple concepts which causes duplication in the standard; - may be interpreted by practitioners as setting requirements that should be specifically addressed in addition to those within the body of the standard; - create potential confusion about the requirement to understand the entity and environment, including the system of internal control that forms the basis of the identification of risks of misstatement versus the identification of inherent risk before consideration of any related controls; and - refer to risks at the assertion level only (from paragraph 4 onwards) and do not refer to financial statement level risks. 	Mainly consistent with feedback from other stakeholders. All points with the exception of point 3 have been included within the AUASB Submission as point 3 was not raised by any other stakeholders.
2	Page 3	R2	No comment.	N/A
3	Page 6	KPMG	We believe that the introductory paragraphs are helpful, as they “set the scene”, help the auditor to navigate this complex standard, and give emphasis to key overarching concepts, including professional scepticism.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
4	N/A	UNSW	No response provided.	N/A
5	Page 3.	ACAG	ACAG agrees that the new introductory paragraphs are helpful.	Consistent with feedback received from other stakeholders. Included in AUASB Submission
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 2 – Are the requirements and application material of ED 01/18 sufficiently scalable, including the ability to apply ED 01/18 to the audits of entities with a wide range of sizes, complexities and circumstances?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 2.	Deloitte	Yes, we note that paragraph A16 indicates: "the auditor's risk assessment procedures to obtain the overall understanding may be less extensive in audits of smaller and less complex entity", and that this has been followed by references to differing requirements for "smaller and less complex" entities in various other paragraphs, as has been highlighted in the IAASB's Explanatory Memorandum. However, the length of the standard may possibly create a challenge in applying this to a very small entity.	Consistent with feedback received from other stakeholders. Included in AUASB Submission
2	Page 4	R2	<p>The proposed standard uses the terms smaller and less complex. Having considered the standard in its entirety it appears the intent of the standard setters and the key driver of risk assessment is complexity and that size while it may be an indicator of complexity is not actually relevant to the complexity of an entity and therefore the risk assessment required. It would be better to simplify the terminology within the standard and simply note that the scalability is dependent on the complexity of a client, because size does not in of itself mean that an entity is not complex. This would simplify some of the other considerations about the language in the standard as to whether smaller and less complex is two distinct populations i.e. smaller clients, population 1, and less complex clients, population 2, or whether it is one population of smaller and less complex entities and to be scalable both elements must be true.</p> <p>Further while scalability is mentioned in the standard there is little guidance as to how to simply and effectively actually scale the effort within the standard, and as a consequence the revised standard will likely lead to greater costs in audit execution.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission
3	Pages 6-7.	KPMG	<p>We are supportive of the overall approach taken by the IAASB regarding scalability of the ED, i.e. the establishment of principles-based requirements, supported by detailed application material, including guidance and examples as to how to apply the requirements across entities that vary significantly in terms of size and complexity.</p> <p>We note that the Explanatory Memorandum, at paragraph 36, states that “clarifying the requirements related to the understanding of each component of the system of internal control is an important aspect of the proposed enhancements to the standard. Within each component, the IAASB has set out the matters that need to be understood, as well as providing further guidance about the extent and scalability of related procedures, as appropriate.”</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>In connection with the above, we welcome, in particular the following enhancements:</p> <ul style="list-style-type: none"> - recognition that aspects of the system of internal control may be less detailed / formalised in smaller and less complex entities; - clarification regarding understanding of the IT environment / identification of risks arising from IT and identification and evaluation of GITCs relevant at smaller and less complex entities; - recognition that complexity as well as, or even more so than, size of an entity is important. We also support the description of smaller and less complex entities being at one extreme, to help provide a reference point as to how the auditor would apply judgement (paragraph A224) and take into account the nature and circumstances of each entity. <p>It would be helpful if the IAASB could provide examples as to the execution of certain requirements. The application material contains theoretical guidance that the nature and extent of procedures may vary according to the audit circumstances, including the size and complexity of the entity subject to audit, but this material would benefit from more detailed examples.</p> <p>Furthermore, the documentation requirements, in their specificity, may be onerous for audits of smaller and less complex entities, as implicitly the judgements in identifying and assessing risks of material misstatement may be difficult to specifically describe. We suggest that the IAASB provide further guidance as to what would be expected in terms of documentation in this area, in particular, the extent to which judgements made en route to a final determination need to be included. We believe it is also critical to clarify the extent of documentation required where, for example, a risk is not significant. While paragraph A245 acknowledges that the auditor is not required to document “every inherent risk factor that was taken into account”, more clarity on the expected extent of documentation will be critical in our view for consistency of application.</p>	
4	N/A	UNSW	No response provided.	N/A
5	Page 3.	ACAG	ACAG considers scalability is limited by using the term “small and less complex” throughout the standard. Complexity is a key factor in determining most aspects of audit risk and audit response. The use of “small or less complex” or “simpler and less complex” would improve scalability as there are large non-complex audits. The public sector has many examples of large non-complex audits, such as policy Departments	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment	ATG Commentary
		<p>where funds are merely administered on behalf of central agencies. Similar examples can exist in the private sector in the form of large controlled entities.</p> <p>We consider that the examples of complexity throughout the ED are well documented however, from our interpretation, an entity will have a de-facto higher risk if it is large and less complex.</p> <p>The definition of “reasonable possibility” is where the likelihood of material misstatement is more than remote. A “remote possibility” is a much lower threshold than “reasonably possible”. If it is intended that “reasonable possibility” and “remote possibility” are not explicitly defined, ACAG suggest further guidance be provided. This can be in the form of criteria for auditors to consider when assessing reasonable possibility versus remote possibility. In the absence of such definitions or clarifying criteria, ACAG questions whether it is the intention for the auditor to apply their professional judgment in making this assessment? Either way, we would support the need for further clarity to aid the auditor in grounding an assessment of “reasonably possible” versus “remote possibility”. In the absence of such guidance, there may be an increase in audit work effort over low risk balances.</p> <p>The requirements in relation to IT risks and response is sufficiently scalable provided the auditor’s skills, experience and knowledge are equally scalable to the level of understanding of the IT environment.</p>	
6	N/A	IIA No response provided.	N/A
7	Page 1.	R7 While the IAASB has stated that it intends the proposed standard to address scalability, we also believe that, as with ISA 540, this standard has again been drafted for entities with complex risks, with the application and other explanatory material being for auditors of entities with less complex risks to guide them in scaling back their audit procedures. This drafting approach means those auditors auditing entities with less complex risks have to read the entire standard to determine what they can exclude from their audit. This is a resource intensive process for SMPs. The preferred approach is to have a base standard for all, then additional material that addresses audit procedures for entities with more complex risks.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Question 3 – Do stakeholders agree with the approach taken to enhancing ED 01/18 in relation to automated tools and techniques, including data analytics, through the use of examples to illustrate how these are used in an audit (see Appendix 1 of the IAASB’s Explanatory Memorandum for references to the relevant paragraphs in ED 01/18)? Are there other areas within ED 01/18 where further guidance is needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 3.	Deloitte	<p>Yes, we agree with the enhancement of ED 01/18 in relation to references to automated tools and techniques, particularly within paragraphs A17-A19, A33 and A48.</p> <p>Another area where further guidance is needed is in relation to the underlying data used within the automated tools and techniques when this constitutes information produced by the entity that is used for risk assessment procedure purposes, and what the requirements are in relation to understanding and/or obtaining evidence over the reliability of this information (including the nature, timing and extent of testing).</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
2	Page 4	R2	<p>The acknowledgement of the use of automated tools and techniques in the standard is a positive addition, although the enhanced wording does not appear to have changed the applicability of these techniques to risk assessment as they were permitted but not expressly mentioned in the extant standard. However, 4 EDs here do not include any revision to ASA 500 and how the such automated tools can be used as a source of audit evidence to respond to risks of material misstatement consistent with ASA 500 para 10.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission with the exception of points around revisions to ASA 500, as this has not been raised by other stakeholders. ASA 500 is planned to be reviewed in 2019-2020.
3	Page 8.	KPMG	<p>We agree with the approach taken and find the illustrative examples helpful. We believe that this is appropriate in terms of the objective of modernizing the standard and making it fit for purpose in today’s technological environment.</p> <p>We are supportive of the approach to avoid the use of terminology that is overly precise/ narrow, or that may be understood differently by various groups, as this is a rapidly emerging field and we recognise the IAASB’s intention not to outdate itself at the outset.</p> <p>However, we suggest that the IAASB further explores the impact of Data and Analytics (D&A) specifically on risk assessment, in terms of whether and how the nature and/or extent of the risk assessment procedures as currently described may change in an audit environment in which the auditor is able to incorporate all transactions into its risk assessment process. As currently described, D&A techniques would appear to be applied in addition to the current requirements of the standard, rather than being an integral part of a possible approach to risk identification and assessment. Paragraphs A33 and A213 touch on this but at a very high level. We recognise that this is an</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			emerging area, and that there is a separate working group/ project to consider the implications of D&A on an audit. However, it would be helpful to further acknowledge this area in the ED.	
4	N/A	UNSW	No response provided.	N/A
5	Page 4.	ACAG	<p>ACAG's overall opinion is that the standard does not include enough information about risk factors relating to the use of big data and automated analytics technology. While these technologies are still evolving, they are evolving at a rapid rate and are widely used throughout the profession, in both private and public sectors. We believe guidance is required now to help the profession address the use of big data and automated analytics technology. There is a risk that the standard, when issued for implementation, will be outdated given the rate of technological evolution.</p> <p>Paragraph 54 (documentation) and paragraphs A15, A18, and A32-A33 discuss that automated tools can be used. However, this application material could be enhanced by:</p> <ul style="list-style-type: none"> - providing information about control assessments over data quality, completeness and accuracy once data is extracted from client systems for use by auditors - commenting on the risk considerations or documentation of judgments specific to the use of predictive analytics or analytic tools that incorporate machine learning or artificial intelligence (AI) by both entities and auditors, particularly the nature of what is considered evidence - providing guidance for documentation of analytic procedures to allow for re-performance where machine learning is used by an entity and/or auditor - outlining clear linkages between the underlying need for quality ITGC assurance and database control assurance prior to the use of automated tools - establishing an expectation about documenting the appropriateness and reliability of external data sets (being data sets external to the entity's sphere of control) - describing how audit analytics and automated tools can be used to assess qualitative inherent risks factors described in section A5. 	Consistent with feedback received from other stakeholders. Included in AUASB Submission. Detailed points not raised by other stakeholders have been included.
6	N/A	IIA	No response provided.	N/A
7	Page 1.	R7	We support the standard explicitly addressing the use of automated tools and techniques. We expect that practitioners would find further application material or implementation guidance useful in relation to these.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Question 4 – Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk identification and assessment process? Do you support the proposed change for the auditor to obtain ‘sufficient appropriate audit evidence’ through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional scepticism?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 3.	Deloitte	<p>In our view ED 01/18 somewhat supports the appropriate exercise of professional scepticism by the inclusion of references to where professional scepticism may be considered or is encouraged, such as within paragraphs A44, A47 and A201.</p> <p>In our view, more explicit references to the expectation and requirement to exercise professional scepticism could be included within the standard, and this could include guidance on the types of procedures to perform, and the associated documentation requirements.</p> <p>We support the proposed change for the auditor to obtain "sufficient appropriate audit evidence" through the performance of risk assessment procedures, however we note that paragraph 54 does not require the auditor to document the procedures performed as part of paragraph 17. It is our view that a requirement to document the procedures performed be included within paragraph 54.</p>	<p>Stakeholders have provided mixed views on the use of the term “sufficient appropriate audit evidence” in ISA 315. The ATG’s view is that the term is inconsistent with terminology already applied in ISA 200, and ISA 500. Therefore the AUASB Submission has recommended using a different term.</p>
2	Pages 4-5.	R2	<p>The change the granularity of risk assessment and terminology will not of itself increase the exercise of professional scepticism, having to perform more work does not in of itself make the executer of that work more sceptical. Scepticism is an attitude and mindset, therefore prescribing that the auditor perform more work does not change the underlying mindset and possibly may even reduce professional scepticism as the auditor is wading through the compliance requirements rather than focusing on exercising their professional scepticism.</p> <p>Use of the term "sufficient appropriate audit evidence" is confusing as it is using a description which is misleading close to that used in ASA 500. Based on the intent of the standard setters for auditors to document their risk assessment processes more fully this could be more meaningfully worded as sufficiently document the risk assessment process or similar wording rather than repurposing the words "sufficient appropriate" and "audit evidence".</p>	<p>Stakeholders have provided mixed views on the use of the term “sufficient appropriate audit evidence” in ISA 315. The ATG’s view is that the term is inconsistent with terminology already applied in ISA 200, and ISA 500. Therefore the AUASB Submission has recommended using a different term.</p>
3	Pages 8-9.	KPMG	<p>Overall, we believe that the proposals are helpful in supporting the appropriate exercise of professional scepticism throughout the risk identification and assessment process. In particular, we agree with the principles-based approach and reference to the concept of professional scepticism in an overarching fashion in the introductory paragraphs, rather than the inclusion of several, individually prescriptive requirements, throughout the standard. We believe that this approach is</p>	<p>Stakeholders have provided mixed views on the use of the term “sufficient appropriate audit evidence” in ISA 315. The ATG’s view is that the term is inconsistent with terminology already applied in ISA 200, and ISA 500.</p>

Item No.	Ref Page No.	Respondent Comment	ATG Commentary
		<p>aligned to the current description of professional scepticism being a mindset/ fundamental behaviour of an auditor.</p> <p>With regard to the proposal to include a requirement in paragraph 17 for the auditor to “obtain sufficient appropriate audit evidence as a basis for the identification and assessment of risks of material misstatement”, we do not consider this concept to be applicable to separate “steps” in this auditing standard. This terminology is understood in a broader context and the proposed approach does not recognise the cohesive nature of an audit as a whole.</p> <p>Accordingly, we suggest that the IAASB considers revising the requirement to remove the reference to “sufficient, appropriate” when describing audit evidence.</p>	<p>Therefore the AUASB Submission has recommended using a different term.</p>
4	Pages 2-3.	<p>UNSW</p> <p>Our own research, and that of others, suggests that the proposals will support the appropriate exercise of professional scepticism throughout the risk identification and assessment process, especially as it relates to fraud risk. In particular, discussions among the engagement team (paragraphs 22, A41-A45) have been shown to result in higher levels of professional scepticism. We feel, however, that additional explanatory material emphasising that the engagement partner should consider the format of the discussion, and how to communicate with those not in attendance at the discussion, would be beneficial in supporting the appropriate exercise of professional scepticism.</p> <p>Paragraph 22 (and the related explanatory material) is silent on the format that engagement team discussions should take. We believe that there is merit in noting that different formats may be more or less effective, depending on the circumstances. Our research (Trotman, Simnett and Khalifa 2009; Chen, Khalifa, Morgan and Trotman 2018; Chen, Trotman and Zhou 2015; Trotman, Bauer and Humphreys 2015), consistent with a number of other studies (e.g., Carpenter and Reimers 2013; Dennis and Johnstone 2018), highlight that differences in the nature and format of the discussion (e.g., face-to-face or electronic brainstorming), and those involved in the discussion, can facilitate or impede a robust risk assessment process. To illustrate, we (Trotman, Simnett and Khalifa 2009) find that different group formats and different instructions to group members affected the number and nature of potential frauds identified. In another study (Chen, Trotman and Zhou 2015), we find that when the discussion takes place via computer interaction (as may be the case when discussion participants are geographically dispersed), discussion impedes the risk assessment process and that this is caused, in part, by less experienced auditors relying on others to provide inputs into the discussion.</p> <p>While supporting the ongoing requirement for audit team members to discuss the potential for material misstatement, we believe that the risk assessment process would be more robust if paragraph 21, in addition to noting that the engagement partner is to determine which matters are to</p>	<p>A summary of academic feedback in relation to this matter has been included in the AUASB Submission.</p>

Item No.	Ref Page No.	Respondent Comment	ATG Commentary
		<p>be communicated to engagement team members not involved in the discussion, also notes that the engagement partner is to use professional judgment to decide the format of, instructions provided, and who will participate, when conducting the discussion. This can also be further elaborated upon in the explanatory material, by noting that the discussion can take many forms and that it is a matter of professional judgment as to what form such discussions should take in order to facilitate a robust risk assessment process.</p> <p>In addition, our own research (Kim and Harding 2017), consistent with other research highlighting that the preferences of the auditor's firm and superior can influence (both positively and negatively) their judgments (e.g., Peecher 1996; Wilks 2002; Shankar and Tan 2006), provides support for a communication plan (noted as being potentially useful in paragraph A45) in order to minimize deleterious consequences of the engagement partner inappropriately directing the risk assessment process, and to leverage off the benefits that such communication can have on elevating professional scepticism in the risk assessment process.</p> <p>We have also undertaken research examining the effect on professional scepticism of differences in what the partner communicates to those not involved in the discussion (Harding and Trotman 2017). This research highlights that the nature of the communication with those not involved in the discussion can have a noticeable effect on the level of professional scepticism exercised by those receiving the engagement partner's communication.</p> <p>Based on this research, we recommend, in order to encourage professional scepticism in the risk assessment process, that paragraph A45 be expanded to note that the engagement partner should be cognisant, when communicating with those not included in the discussion, that what they communicate, and how they communicate, might lead to auditor bias which can, depending on the circumstances, both positively and negatively impact the level of professional scepticism being exercised.</p> <p>Also with reference to the exercise of an appropriate level of professional scepticism, we draw attention to recent developments in the academic literature regarding the representation of professional scepticism. The academic literature has, of late, addressed professional scepticism as both a mindset and an attitude (see Nolder and Kadous 2018). Broadly speaking, mindsets (i.e., "judgment criteria and cognitive processes and procedures to facilitate completion of a particular task") directs an auditor's approach to risk assessment, and attitudes (i.e., beliefs and feelings that drive individual intentions and actions") direct an auditor's response to that risk assessment. Both mindsets and attitudes are important in encouraging and supporting an appropriate level of professional scepticism.</p>	

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>With reference to mindsets, the understanding of professional scepticism in the extant standards is consistent with a deliberative mindset that "...is characterized by receptivity, openness or alertness to new information, and an objective and unbiased assessment of the merits of the evidence" (Nolder and Kadous 2018, p.5). Attitudes, by comparison, refer to beliefs and, importantly, feelings that will influence future actions (e.g., response to an identified risk of material misstatement). While the current version of the proposed auditing standard goes some way to encourage and support an appropriate sceptical mindset and attitude, there may be opportunities for further improvements.</p> <p>We support reference to contradictory evidence / information in paragraphs A19, A42 and A44 in that the search for and consideration of contradictory evidence is indicative of the exercise of professional scepticism (including the identification of troubling patterns). However, in order to further encourage an appropriate level of professional scepticism, we recommend that thought be given to expanding paragraph A19 to refer to broad sources of information (that may include but not limited to the points noted) so as to avoid consciously and/or subconsciously narrowing the breadth of information search. Similarly, we note that particular reference is made to the consideration of contradictory evidence in paragraph A42 and suggest that other benefits of the engagement team discussion can be noted, including helping auditors to be open to new information, and different interpretations of the information, and to limit the possibility of prematurely forming a belief.</p>	
5		ACAG	<ul style="list-style-type: none"> - ACAG considers the prompts to consider professional scepticism are sufficient. We support the emphasis on "management bias", particularly the link to the entity's financial performance. We consider the most important encouragement of professional scepticism is behavioural change through staff awareness and training. - ACAG supports the emphasis on an appropriate evidence base for risk assessment. If quality evidence is not found to be available at an early stage, the auditor should become more sceptical, continue to challenge management and refine the audit approach as required. <p>While ACAG supports the intention of this change, we are concerned that the specific requirement for the risk assessment procedures to obtain sufficient appropriate audit evidence as the basis for identification and assessment of risks is unclear. The objective of an audit of financial statements is to draw conclusions on the financial statements as a whole and not on the risks of material misstatement. Risk assessment procedures and other audit procedures work together to allow the auditor to obtain a sufficient and appropriate evidence on which to draw conclusions because audit evidence is cumulative in nature. That is to say, sufficiency and appropriateness of evidence can only be measured when concluding on the subject matter and</p>	Stakeholders have provided mixed views on the use of the term "sufficient appropriate audit evidence" in ISA 315. The ATG's view is that the term is inconsistent with terminology already applied in ISA 200, and ISA 500. Therefore the AUASB Submission has recommended using a different term.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			risk assessment procedures alone may not be able to draw conclusions. For example on a practical level, when taking a controls strategy, the auditor will not have sufficient and appropriate audit evidence of control risk at the conclusion of the risk assessment phase of the audit because procedures related to assessing the operating effectiveness of controls is a risk response procedure. The risk assessment procedures for controls only provide an educated guess as to the likely results of the testing which is not consistent with sufficient and appropriate audit evidence. Similarly, the emphasis on the iterative nature of risk assessments also suggests that the sufficiency and appropriateness of evidence related to risk assessment relies upon the corroboration of the execution of the risk response.	
6	N/A	IIA	No response provided.	N/A
7	Page 1.	R7	We support the inclusion of more detail on professional scepticism, although there is potential for this to be taken further. The standard does not contain much more than the extant standard in relation to documentation, and this is often the aspect of the exercise of professional scepticism that regulators identify as lacking.	Stakeholders have provided mixed views on the use of the term “sufficient appropriate audit evidence” in ISA 315. The ATG’s view is that the term is inconsistent with terminology already applied in ISA 200, and ISA 500. Therefore the AUASB Submission has recommended using a different term.

Question 5 – Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks or material misstatement? Specifically:

Qn. 5(a) – Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 3.	Deloitte	<p>Yes, the additional guidance in the latest exposure draft enhances the understanding of what is required of the auditor in documenting the components of the entity's system of internal control. Additionally the updated definitions provide greater relevancy and clarity.</p> <p>We note that different paragraphs convolute the consideration of the entity's controls with respect to the identification and assessment of risks of material misstatement. Some of these paragraphs are included within the "Key Concepts in this ASA" section, so they are critical for auditors to understand when applying the standard.</p> <p>Within paragraph 4, it states "The required understanding of the entity and the environment, the applicable financial reporting framework, and the system of internal control forms the basis for the auditor’s identification of risks of material misstatement. The identification of risks of material misstatement at the assertion level is performed before consideration of any controls."</p> <p>Paragraph 39(e) states:</p> <p>[The auditor shall identify controls relevant to the audit. being those:] That, in the auditors professional judgement, are appropriate to evaluate their design and determine whether they have been implemented to enable the auditor to:</p> <p>Identify and assess the risks of material misstatement at the assertion level; or</p> <p>Design further audit procedures responsive to assessed risks.</p> <p>The "Identifying and Assessing the Risk of Material Misstatement" flowchart also supports the view that the understanding of controls is factored into the process to identify risks of material misstatement.</p> <p>We believe the first point that needs to be made clear is the identification of a risk of material misstatement versus the assessment of a risk of material misstatement. The next point is in relation to differentiating between having an 'understanding of internal control' (as included in paragraph 4) when identifying risks of material misstatement versus assuming that the entity's controls are operating effectively and thus influencing whether a risk of material misstatement exists or not.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>Ultimately, the understanding of the internal control structure including the design and implementation of controls is appropriate and required when identifying and assessing risks of material misstatement, however auditors are unable to conclude that there is a remote risk (therefore not a risk of material misstatement) by assuming that one or more controls are operating effectively - this is what needs to be clearly communicated within the standard.</p> <p>Thirdly, it is unclear how inherent risk and control risk interacts and combines together when it comes to assessing the risks of material misstatement.</p> <p>For instance, paragraph 5 states "For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk and control risk is required by this ASA." However no requirements or guidance is provided on how these separate assessments then combine together to form the overall assessment of the risk of material misstatement.</p>	
2	Page 5.	R2	<p>In conjunction with the flow chart "obtaining an understanding to the entity's system of internal control" the revised standard clarified the understanding of what is required and how it feeds to the risk assessment. In particular the limiting of the design and implementation testing to the information system and communications, and the control activities. The inclusion of the flow charts will be crucial in appropriate adoption and understanding of the standard both by practitioners and regulators.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
3	Pages 9-11.	KPMG	<p>We are supportive of the IAASB's aims in enhancing and clarifying this area, as we consider that much of the complexity and scope for inconsistency of application in practice lies in obtaining this understanding. In particular, we welcome the alignment of the categorisation of the components of the system of internal control to the COSO Framework, and therefore the order in which the components of internal control are presented. Additionally, the requirements include greater focus on why we obtain the understanding, with a number of "signposts" or "milestones" that require the auditor to make an evaluation.</p> <p>However, we suggest that the IAASB consider clarifying that any 'evaluation' is made in respect of the overarching objectives of the standard as a whole, and not in respect of any specific matter in isolation.</p> <p>We believe there is scope for inconsistency in application in relation to how to obtain the required understanding of each component of the system of internal control, which may present challenges for auditors of smaller and less complex entities in particular.</p> <p>For example, we believe there is an intentional difference in respect of the understanding obtained over the information system and communication component of the system of internal control, and that an auditor is required to identify the controls relevant to financial reporting that are embedded in this component and to evaluate the design of this system by evaluating the design and implementation of</p>	<p>Consistent with feedback received from other stakeholders. Included in AUASB Submission.</p> <p>Specific points for improvement have not been raised by other stakeholders and have not been included.</p>

Item No.	Ref Page No.	Respondent Comment	ATG Commentary
		<p>these controls, but is not required to perform a similar evaluation in respect of the controls in the other components, other than to identify whether there are any controls relevant to the audit within these components. We suggest that the IAASB clarify whether this is an intentional difference.</p> <p>We believe that the ED may give rise to uncertainty and inconsistency in application with regards to the understanding that is required to be obtained in respect of the information system and communication component of the system of internal control at paragraph 35(a)–(d) and how this relates to the evaluation of the design and implementation of the information system controls relevant to financial reporting required by paragraph 36. It is unclear whether the requirement at paragraph 36 is achieved through the performance of paragraph 35, or whether it is considered as part of the performance of paragraph 35. This is compounded by a lack of clarity as to how this understanding is obtained.</p> <p>Furthermore, we are concerned that the ED does not sufficiently clarify which controls reside in the information systems component and which in the control activities component and how these interrelate, if at all.</p> <p>At paragraph 37 of the EM, the IAASB notes that “Controls relevant to the audit are primarily direct controls and controls in the controls activities component. However, the auditor may identify certain controls in the control environment, the entity’s risk assessment process or the entity’s process to monitor controls as relevant to the audit because they address risks of material misstatement at the assertion level.”</p> <p>The above leads to a lack of clarity as to the distinction between the nature of the controls in the information system component and the control activities component, including whether controls over the flow of information are direct and why controls in the information system component are relevant to financial reporting whereas controls in the control activities components are relevant to the audit, and how these concepts are connected. There is also uncertainty in relation to the work needing to be performed over controls that are relevant to financial reporting.</p> <p>We consider that the standard would particularly benefit from clearer linkage between the “understanding” obtained regarding each of the components of the entity’s system of internal control and how this is applied in fulfilling the requirements to identify and assess the risks of material misstatement at paragraph 45 onwards. Paragraph 17 describes this understanding as forming the basis for the risk identification and assessment. However, the application material, in particular A201 and A202, focuses more on the inter-relatedness of these aspects of the standard, e.g. that the auditor forms initial expectations and then confirms or updates these, or that information gathered in performing the risk assessment procedures to obtain the understanding is used as audit evidence to support the risk assessment. Paragraph A208 states that the identification of risks of material misstatement at the assertion level is performed before consideration of any controls, which seems to</p>	

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			contradict this linkage insofar as risks of material misstatement at the assertion level are concerned. The reference to “significant classes of transactions, account balances and disclosures” in the requirement at paragraph 35(a), in relation to the understanding of the information system relevant to financial reporting, also seems to contradict the notion that the understanding of this component of internal control is considered in identifying the risks of material misstatement, i.e. significant classes of transactions, account balances and disclosures).	
4	N/A	UNSW	No response provided.	N/A
5	Page 6.	ACAG	This aspect is enhanced and clarified and shows the link to risk identification. ACAG is supportive of the clarification that when the operating effectiveness of controls are not tested, the auditor shall assess control risk at the maximum.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 5(b) – Have the requirements related to the auditor’s identification of controls relevant to the audit been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 4.	Deloitte	<p>Paragraph 39 and the associated guidance paragraphs have enhanced the standard, however we don't believe that they have provided a lot of clarity on what constitutes other controls relevant to the audit, and the expectations and requirements on how the auditor determines these. We acknowledge there is some enhanced guidance within paragraph A179 however this doesn't extend to providing clarity on how the auditor may go about determining what other controls are relevant in the circumstances.</p> <p>Similarly, paragraph A167 indicates that for smaller and less complex entities, there may not be any other controls aside from the minimum expectation of controls over journal entries, however does not provide guidance on how the auditor should exercise professional judgement in making this determination. It also doesn't contemplate the common situation for smaller and less complex entities where controls exist but are not formally documented.</p>	Consistent with feedback received from other stakeholders with the exception of the second point. Only the first point has been included in AUASB Submission.
2	Pages 5-6.	R2	<p>The revised standard increases the clarity of selecting the relevant controls in particular in Para A166 and A167, is clear that the auditor may, based on their judgement of the complexity and size of an entity conclude that the only relevant controls are those over journal entries if they do not plan to rely on any of the other controls which may be present. However, there is much less clarity over what constitutes a smaller and less complex entity, while assuming this is intentional to encourage auditors to consider the client, it is also open to considerable misinterpretation or variability of interpretation as to what is smaller and less complex.</p> <p>The revised standard however, is likely to result in far more controls being considered relevant because of the definition of relevant assertions being described in the introductory paras as being "reasonably possible" whereas the language in the standard in the definitions in para 16 (h) describes reasonably possible as being where this is more than remote.</p> <p><i>(h) Relevant assertions -An assertion is relevant to a class of transactions, account balance or disclosure when the nature or circumstances of that item are such that there is a reasonable possibility of occurrence of a misstatement with respect to that assertion that is material, individually or in combination with other misstatements. There is such possibility when the likelihood of a material misstatement is more than remote. The determination of whether an assertion is a relevant assertion is made before consideration of controls. (Ref Para, A9)</i></p> <p>This wording seems to be the inverse of the intent of the standard setters which according to the discussions at the round table was to suggest that remote mean reasonably possible, in ordinary use this might be interpreted as more likely than not, but the wording in the standard is to suggest that</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>reasonably possible is measured as being greater than remote, the exact opposite or the outlined intent of the standard setters. Remote has the implication in ordinary use of being highly unlikely, implausible, far-fetched, therefore the use of the word in the standard is misleading or will result in most balances and most or all assertions being considered to have a risk greater than remote and therefore being relevant. Hence, relevant controls will necessarily be greater in response to more assertions being considered relevant.</p> <p>The issues of the use of the word remote and the definition of relevant assertions is likely to lead to more controls being identified which is going to make scaling the standard for "smaller and less complex entities" more challenging.</p>	
3	Page 11.	KPMG	<p>We welcome the additional granularity regarding the types of controls that are relevant to the audit in paragraph 39. We also find the clarification in the application material that most controls, although not necessarily all, that are relevant to the audit will be direct controls, and that these will reside in the Information System and Communication, and Control Activities components, helpful.</p> <p>Notwithstanding the above, this is a complex area. We recommend that the IAASB introduce further clarity regarding paragraph 39(e), which refers to controls for which it is appropriate to evaluate their design and determine whether they have been implemented to enable the auditor to identify and assess the risks of material misstatement at the assertion level. This is difficult to implement – how can you “know what you don’t know” unless you identify and evaluate all the controls. We believe that this concern applies irrespective of the size or nature of the entity, although the work effort to identify these controls may seem disproportionate in a smaller entity.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
4	N/A	UNSW	No response provided.	N/A
5	Page 6.	ACAG	The process for identification of relevant controls is enhanced and clarified and consider this can be applied to all types of audits.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 5(c) – Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor’s understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor’s consideration of the effects of the entity’s use of IT on the identification and assessment of the risks of material misstatement?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 4.	Deloitte	<p>a) Yes, we support the introduction of the new IT-related concepts and definitions as they provide a baseline understanding for auditors.</p> <p>The enhanced requirements and application materials around the impact of the IT environment and IT controls on the identification and assessment of risks of material misstatement is useful in assisting the auditor to understand the various elements of what is required as part of the risk assessment process.</p> <p>b) Having said this, we highlight that it is a requirement under paragraph 38 that the auditor obtains an understanding of the control activities component - how this interacts with risk identification and assessment is unclear particularly in the context where the identification of risks of misstatement is made before the consideration of controls (refer to our response to question 1(a) and our comments in Appendix 2).</p>	<p>Point a) consistent with feedback received from other stakeholders. Included in AUASB Submission.</p> <p>Point b) has not been raised by other stakeholders so not included.</p>
2	Page 6.	R2	The enhancements to the standard certainly make clearer the requirements, however there is also an implied increase in the volume of expected work from the extant standard.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
3	Page 11.	KPMG	<p>We support the introduction of the new IT-related concepts and definitions and agree that these are necessary to ensure that ASA 315 remains fit for purpose in a modern environment.</p> <p>In respect of the IT environment, we note that the description/ definition at A7 and A8 is very technical and may not be clearly understood by auditors.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
4	N/A	UNSW	No response provided.	N/A
5	Page 6.	ACAG	<p>ACAG supports the introduction of IT related concepts and definitions.</p> <p>ACAG’s overall opinion is that the standard does not include enough information about risk factors relating to current and quickly evolving technology, such as “infrastructure/ software as a service” solutions, wireless networks, blockchain, and other technology devices (Internet of Things) that connect to organisational networks. These are current technologies that are being used in organisations now, including many public sector organisations.</p>	ATG has included the points relevant to risk factors, in the AUASB Submission. Other points have not been have not included as they relate to specific technology and tools and may become obsolete.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>We note:</p> <ul style="list-style-type: none"> - the enhanced material is only sufficient for simple in-house IT environments; - understanding the transaction flow for significant classes of transactions, account balances and disclosure COTBAD is an important step and will highlight all the systems involved. However, auditors will need more guidance in understanding “as a service” offerings within the IT environment and the related risks of trusted third parties; - more guidance is required to understand the end-to-end IT services that relate to processing significant COTBAD for comprehensively identifying and assessing risks resulting from the use of IT; - use of other new technologies, such as Distributed Ledger Technology (including block chain), also present different and additional risks to the control environment that need to be considered when understanding the IT environment. 	
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 6 - Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:

Qn. 6(a) – Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments’?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 4.	Deloitte	<p>a) Yes, we support the separate assessments of inherent and control risk to the extent of preventing auditors from "taking credit for controls" when determining risks of material misstatement, however we believe that there is a need to clearly articulate the consideration of controls when assessing inherent risk (that is, using the understanding of the control environment and internal controls that exist) and what is included within the assessment of inherent risk versus control risk (for example, where the entity does not have an appropriate control or the control is not designed or implemented appropriately, whether this is incorporated as part of the inherent risk or control risk assessment).</p> <p>Furthermore, in the introduction paragraphs it states that the assessment of the risks of material misstatement at the assertion level are based on the separate assessments of inherent risk and control risk, however there is no clarity or guidance on how the combination of these separate assessments come together when determining the risk of material misstatement. Following on from this, it is highlighted that control risk would be assessed at "maximum" if the auditor does not intend to rely on the operating effectiveness of control(s) that address the risk of material misstatement, however there is no linkage or connection to the understanding of the control environment and the design and implementation of these controls (which we assume is part of the inherent risk assessment, although this is not directly stated).</p> <p>Refer to our detailed comments within Appendix 2.</p> <p>b) The requirement to assess control risk at less than maximum automatically, based on the planned audit strategy does not take into consideration the underlying robustness of the control and whether they will prevent, detect or correct material misstatements, as defined in Paragraph 3.</p> <p>c) Additionally, the requirement to assess control risk at less than maximum based on the planned audit approach, may not be always be appropriate. Paragraph 53 states:</p> <p>“The auditor's assessments of the risks of material misstatement at the financial statement level and assertion level may change during the course of the audit as additional audit evidence is obtained.”</p> <p>which is one example where the control risk may be set at maximum notwithstanding the planned</p>	<p>Points a) and b) consistent with feedback received from other stakeholders. Included in AUASB Submission. Point c) is inconsistent with other feedback received from stakeholders and has not been included.</p>

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			audit approach.	
2	Pages 6-7. Page 11.	R2	<p>We support the separation of inherent risk and control risk. However, the use of the term control risk is confusing and misleading. The control risk is a response not a risk i.e. it is binary in its outcome in respect of audit evidence, either the control is tested or it is not i.e. there is audit evidence or there is not, the extent of the audit evidence from a tested control. Therefore, it is not possible to not test controls and conclude that a risk of material misstatement does not exist if the inherent risk suggests it is a risk of material misstatement. Therefore, it is unclear how any factor in substance affects the determination of risks of material misstatement other than the inherent risk. The response can be either controls, or substantive tests or a combination but the inherent risk i.e. the risk of material misstatement cannot by definition be reduced without testing the controls, therefore controls do not determine inherent risk controls are a mechanism to respond to inherent risk, as inherent risk does not include controls as an inherent risk factor.</p> <p>A5 and A6 - Para A5 is the inherent risk factors but para A6 reads like another list of inherent risk factors either they are all risk factors and should be in a single para or para A5 is a little misleading in describing it as "the" inherent risk factors.</p>	Point raised in relation to assessing control risk and more guidance has been included in AUASB Submission. Other points not consistent with feedback from other stakeholders. Para 16f refers to paras A5 and A6, therefore considered clear.
3	Page 12.	KPMG	<p>We support the separate assessments of inherent and control risk at the assertion level, and we consider that the related requirements and guidance are clear. We believe this amendment results in better alignment to ASA 330.7, which requires the auditor to consider inherent risk and control risk separately in order to respond, and it also aligns to the amendments already made to ISA 540 in this regard.</p> <p>As discussed above, we suggest that the IAASB consider whether the concept of 'identification of a risk of material misstatement' (versus assessment of a risk of material misstatement) can be dropped, given the separation of assessments of inherent and control risk.</p>	Paragraph 1 consistent with feedback from other stakeholders and has been included in AUASB Submission. Paragraph 2 not consistent, has not been raised in submission.
4	Pages 3-4	UNSW	Although not specifically related to separate assessments of inherent and control risk, we (Chen Khalifa and Trotman 2015) find that auditors identify more potential frauds when sequentially considering one risk area at a time (e.g., revenue recognition/receivables, inventory, non-current assets and management estimates). If applied to the unpacking of risk of material misstatement assessments (and we have no reason to expect that our findings would not be applicable), these findings suggest that separate assessments of inherent risk and control risk would result in the identification of more risk factors and a more robust risk assessment process. We therefore support the separate assessment of inherent and control risk.	Feedback not consistent with other stakeholders, has not been included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			As a word of caution, however, while more fraud risk factors were identified, auditors in our study assigned a lower likelihood to these fraud risk factors, suggesting that lower levels of scepticism may accompany the ‘unpacking’ of assessments of risk of material misstatement. Simon, Smith and Zimbleman (2018) similarly report that decomposition of fraud risk assessments into likelihood and magnitude components (compared to a holistic assessment) led auditors to “...discount their fraud risk assessment for higher-risk fraud schemes”(p.3). These results suggest that while unpacking/decomposing the risk of material misstatement may be beneficial by way of increasing auditors’ sensitivity to information, it may limit the scepticism applied to the risks identified. We therefore recommend that the application and other explanatory material relating to paragraph 48 be expanded to reinforce the need to exercise an appropriate level of scepticism across the greater number of identified risks that are likely to follow from the unpacking / decomposition of the components of risk of material misstatement assessments.	
5	Page 7	ACAG	ACAG supports the separate assessment of inherent and control risk and agrees the revised requirements and guidance are appropriate.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 6(b) – Do you support the introduction of the concepts and definitions of ‘inherent risk factors’ to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor’s risk assessment process?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 5.	Deloitte	Yes, we support the introduction of these concepts and definitions. However we note that whilst the factors have been established, they are quite high level and how the auditor applies these factors against a spectrum of risk assessment has not been explained, nor guidance provided.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
2	Page 7.	R2	The inherent risk factors are consistent with what an experienced auditor might use and essentially consistent with the factors previously described in the extant standard for a significant risk, however the revised standard makes clear that the presence of these factors is not binary but a scale and that a risk of material misstatement can have some of these factors and still not be a significant risk. This is a better reflection of the audit environment than the extant standard. The practical execution of these factors however and the expectations of documentation of each factor is unclear. If each risk is expected to have detailed documentation for each factor then the changed standard will result in an extremely burdensome documentation requirement, a better understanding of regulatory interpretations of this would allow a more considered response to this.	Consistent with feedback received from other stakeholders. Included in AUASB Submission. Point on documentation is included in application material of ED, para A245.
3	Page 13.	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 7.	ACAG	ACAG supports the concepts of inherent risk factors and agrees the guidance is appropriate.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 6(c) – In your view, will the introduction of the ‘spectrum of inherent risk’ (and the related concepts of assessing the likelihood of occurrence, and magnitude, of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 5.	Deloitte	<p>This formalises a concept that auditors have already been utilising, however more guidance is needed in the application of professional judgement if consistency in the identification and assessment of the risks of material misstatement and significant risk is to be achieved, as currently the implementation guidance only indicates what to look for, rather than how to assess. The term "spectrum" itself has not been defined, nor is guidance included.</p> <p>In addition, there does not appear to be a similar spectrum concept for the control risk assessment - the standard describes only "maximum" and "less than maximum". These options are not clearly defined either, and application guidance is not included.</p> <p>Magnitude is a new way of thinking and can be misinterpreted without specific guidance. Auditors are used to "material" and "significant" and thus magnitude needs to be defined.</p>	<p>Consistent with feedback received from other stakeholders. Included in AUASB Submission.</p> <p>Note on control risk assessment has been included in AUASB submission.</p>
2	Pages 7-8.	R2	<p>The concept of the spectrum of risk is consistent with auditor practice, however the outcome is ultimately still only 2 outcomes, not risks of material misstatement, risks of material misstatement and significant risks. The inclusion of likelihood and magnitude in addition to the inherent risk factors is confusing as adds an alternative method of determining the inherent risk without being included within the inherent risk making the entire decision more complex. The separation and express requirement to consider the factors and to consider likelihood and magnitude in our opinion increase complexity and documentation requirements without substantially impacting risk assessment or audit quality. Auditors may expend considerable time documenting where on the spectrum a matter sits only to ultimately conclude that it is a risk of material misstatement and then determine what work they will do for that risk.</p>	<p>Not consistent with feedback from other stakeholders. Has not been included in the AUASB Submission.</p>
3	Page 13.	KPMG	<p>We are supportive of the introduction of the “spectrum of inherent risk” and believe that this will help us to understand that this may vary smoothly, rather than being the binary assessment of significant versus non-significant that we make at present. We are also supportive of the IAASB’s conclusion to retain the concept of significant risk on the basis that other ISAs contain the concept of significant risk and therefore ISA 315 needs to align to this.</p> <p>Together with the updated definition of significant risk, the concept of a spectrum of inherent risk helps the auditor to focus on the nature of the risks themselves, rather than requiring a determination as to whether a risk is significant based on the expected audit response, i.e. whether the risk requires “special audit consideration”.</p>	<p>Consistent with feedback received from other stakeholders. Included in AUASB Submission.</p> <p>Inconsistent feedback on likelihood and magnitude discussed in submission.</p>

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>We support the IAASB's preliminary conclusion that significant risks are best represented by a high likelihood of occurrence or high magnitude of potential misstatement (rather than 'and'), and consider that the auditor will apply its professional judgement as to whether a matter is actually a significant risk.</p> <p>However, we have some concerns about the description in A229 that significant risks are "assessed close to the upper end of the spectrum" and suggest referring instead to "at the upper end of the spectrum".</p>	
4	N/A	UNSW	No response provided.	N/A
5	Page 7.	ACAG	<p>ACAG agrees with the concept of a "spectrum of inherent risk" and the combined assessment of "likelihood" <u>or</u> "magnitude" when determining significance. We suggest the inclusion of a diagrammatic representation to highlight how likelihood and magnitude interplay in the process of determining if a risk is significant or otherwise, i.e. "likelihood" on one axis and "magnitude" on the other axis.</p> <p>To ensure appropriate determination of "significant risk", ACAG suggests additional guidance be inserted to help auditors determine where on the scale of likelihood and magnitude would result in a significant risk, i.e. would a low likelihood and high magnitude instance result in a significant risk?</p>	<p>Consistent with feedback received from other stakeholders. Included in AUASB Submission.</p> <p>Inconsistent feedback on likelihood and magnitude discussed in submission.</p>
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 6(d) – Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e., an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion), and how they assist the auditor in identifying where risks of material misstatement exist?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Pages 8 & 10.	Deloitte	<p>Significant class of transactions, account balance or disclosure</p> <p>We question why the introduction of a new concept 'significant class of transactions, account balance or disclosure' is required and how it differs from a material class of transactions, account balance or disclosure referred to in ASA 330.</p> <p>Paragraph 4 states:</p> <p>"the assertions to which such risks of material misstatement relate are referred to as 'relevant assertions,' and the classes of transactions, account balances and disclosures to which the relevant assertions relate are referred to as 'significant classes of transactions, account balances and disclosures.</p> <p>Intuitively we would equate a significant class of transactions, account balance or disclosure to be the same as a material class of transactions, account balance or disclosure as fundamentally it comes down to the existence of one or more risks of material misstatement associated with one or more relevant assertions, however this is not how it is currently structured.</p> <p>Paragraph 10 indicates that:</p> <p>"After identifying_ the risks of material misstatement, the auditor determines the significant classes of transactions, account balances and disclosures.</p> <p>The auditor is also required to perform a stand-back to confirm that this identification is appropriate."</p> <p>Similarly paragraph 46 requires that:</p> <p>"The auditor shall determine significant classes of transactions, account balances and disclosures, and their relevant assertions, based on the identified risks of material misstatement."</p> <p>It appears that a significant class of transactions, account balance or disclosure is a subset of a material class of transactions, account balance or disclosure (i.e. a significant class of transactions, account balance or disclosure is always a material class of transactions, account balance or disclosure, but not vice versa), but this is not clearly defined and the concepts/definitions are not currently articulated to distinguish between them.</p>	<p>Para 4 included in submission.</p> <p>Other feedback inconsistent with other stakeholders, not included in AUASB Submission.</p>

Item No.	Ref Page No.	Respondent Comment	ATG Commentary
		<p>The inclusion of a significant class of transactions, account balance or disclosure within ASA 315 is misleading and confusing as there is no clear distinction between this and a material class of transactions, account balance or disclosure.</p> <p>As a consequence, it is unclear what the expectation of the auditor is under Paragraph 10 and 46.</p> <p>Relevant assertion</p> <p>We recommend that consideration factors or additional guidance be linked or included, in order to assist auditors in determining what constitutes a 'reasonable possibility' or when a possibility would be 'remote'.</p> <p>In addition, this paragraph states that the "determination of whether an assertion is a relevant assertion is made before consideration of controls", which implies that relevant assertions are only applicable to inherent risk and not control risk. This does not envisage scenarios such as when the entity does not have a control over the cut-off assertion, or they do have a control but it is not designed/implemented appropriately. This may potentially lead to an additional relevant assertion (if cut-off was not considered relevant beforehand) that is based on control risk not inherent risk. If this is considered to be part of the inherent risk assessment rather than control risk assessment, then this needs to be made clear so that it sets the scene for the remainder of the standard.</p>	
2	Page 8.	<p>R2</p> <p>Refer previous comments about the misleading definition of reasonable possibility being anything more than remote in response 5b.</p>	<p>Consistent with feedback received from other stakeholders. Included in AUASB Submission.</p>
3	Page 13.	<p>KPMG</p> <p>We are supportive of the inclusion of the new concepts and related definitions, however, we recommend that the IAASB provides further information to support the definitions, such as examples of “classes of transactions” and “account balances” and the distinction between the two.</p> <p>We note that one of the intentions of the IAASB is to clarify the scope of the auditor’s understanding of the information system, and the auditor is required at ED 01/18.35(a) to “understand how information relating to significant classes of transactions, account balances and disclosures flows through the entity’s information system.” We believe that this is helpful as it clarifies when such understanding needs to be obtained.</p> <p>We also support revisions to the definition that better focus on a significant risk being assessed by reference to the spectrum of inherent risk, rather than on the response to the risk. It better enables</p>	<p>Inconsistent with feedback from other stakeholders. Not included in AUASB Submission.</p>

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			compliance with the requirement in the extant standard at paragraph 27 to identify significant risks excluding the effects of controls, i.e. based on the inherent risk alone.	
4	Page 4	UNSW	<p>The definition of relevant assertion refers to "... a reasonable possibility of occurrence of a misstatement with respect to that assertion that is material ..." In the definition, this is subsequently explained as "...the likelihood of a material misstatement [that is] more than remote". The definition of relevant assertion, envisages that the terms 'reasonable possibility' and 'more than remote' are equivalent. Indeed, in the IAASB Explanatory Memorandum to ED315 (footnote 26), it is noted that the "IAASB is of the view that the two terms are synonymous". Research would suggest that this is not the case, and equating reasonable possibility with more than remote will likely lead to confusion.</p> <p>In 2016, the Korea Accounting Standards Board and the Australian Accounting Standards Board reported the results of a survey eliciting Korean and Australian preparers' and auditors' interpretation of linguistic probability statements contained in the International Accounting Standards. Australian preparers and auditors perceived remote to mean a probability of 9.0% (range 3.2% to 12.1%). However, these same preparers and auditors perceived reasonably possible to mean a probability of 57.2% (range 49.7% to 72.7%). Similar results are revealed in Amer, Hackenbrack and Nelson (1994), that is; remote: 12.33%, reasonably possible: 58.57%. There are, therefore, a broad range of likelihoods (approximately 10% to 50%) that, while being more than remote, are not reasonably possible. This difference between more than remote and reasonable possibility highlights the dangers in attempting to define one linguistic probability term with reference to another linguistic probability term, and this is even more the case when the terms are clearly perceived to be different. Between remote and reasonably possible in the joint KASB/AASB study were, from less likely to more likely; extremely unlikely, highly unlikely, unlikely and possible. We would not recommend defining one linguistic probability statement in terms of another.</p> <p>Whether the term 'reasonable possibility' or 'more than remote' is employed rests on standard setters' preference for the standard to capture more or less assertions. The term 'more than remote' will capture more assertions than 'a reasonable possibility'. We do not offer any comment on which of these two terms is better.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
5	Page 7-8.	ACAG	ACAG is not clear as to the intention of the introduction of this concept as there is minimal guidance as to the difference in auditor response to significant COTABD and material COTABD. Para A242 requires the auditor to address quantitatively and qualitatively material COTABD in accordance with ISA 330 para 18 which states that "the auditor shall design and perform substantive procedures...."	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>In order to design and perform audit procedures, the auditor would first need to determine the relevant assertion at risk. If that is the case, then ACAG questions the appropriateness of the auditor's response to material COTABDs.</p> <p>Given the example provided in para A242 refers to a qualitatively material disclosure, it appears the intent to distinguish between significant and material is related to qualitatively material aspects of the COTABD. ACAG questions the benefits of making this distinction if this is the case, as the concept of qualitatively material COTABD is an existing concept and auditors would already be considering the qualitative aspects under the current framework when scoping in their COTABDs.</p>	
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 6(e) – Do you support the revised definition, and related material, on the determination of ‘significant risks’? What are your views on the matters presented in paragraph 57 of the IAASB’s Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 5.	Deloitte	<p>Yes, the previous definition of significant risks within the extant ISA 315 focused on the response to a significant risk, rather than defining what a significant risk is. Whilst we agree with defining significant risks as relating to inherent risk close to the upper end of the risk spectrum, we highlight the fact that this does not consider situations where significant risk may arise due to inherent risk being exacerbated by issues with internal controls. In addition, linking to our response to question 6(b) above, the risk spectrum is not defined and no further guidance is included to assist in understanding the concept of the "upper end" of the spectrum.</p> <p>The definition of a significant risk is an identified risk of material misstatement for which the inherent risk is close to the upper end of the spectrum of inherent risk. The potential impact of the control risk is not referred to at all.</p> <p>Does this mean that only the inherent risk impacts whether a risk of material misstatement is classified as significant or not? Our view is that the potential for a significant risk may be increased if the entity does not have relevant controls or they were not designed, implemented or operating effectively.</p>	Point on spectrum of inherent risk is included. Other points inconsistent with feedback from other stakeholders. Not included in AUASB Submission.
2		R2	The concept that significant risks can be determined by either magnitude or likelihood, is confusing in two aspects: Firstly the use of or, it would appear that it’s a combination of magnitude and likelihood which would drive a risk to be considered significant. Secondly, the risk is defined by its inherent risk factors and it’s the extent to which they are applicable which would determine whether an inherent risk is significant. As such there is insufficient clarity as to the application and use of the likelihood and magnitude in conjunction with the inherent risk factors to determine whether a risk is significant.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
3	N/A	KPMG	No comment	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 8.	ACAG	ACAG supports the revised definition and related material on determining risk. We are aware of examples such as IT environments where the likelihood of a risk is low, but the consequence extremely high. Therefore, it is important not to exclude these risks from the auditor’s determination of significant risks.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
6	N/A	IIA	No response provided.	N/A

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
7	N/A	R7	No response provided.	N/A

Question 7 – Do you support the additional guidance in relation to the auditor’s assessment of risks of material misstatement at the financial statement level, including the determination about how, and the degree to which, such risks may affect the assessment of risks at the assertion level?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 6.	Deloitte	<p>We support the need for additional guidance in relation to the auditor's assessment of risks of misstatement at the financial statement level. We note however that the guidance within ED 01/18 is largely centered on the risk of misstatement at the assertion level. ED 01/18 does not contain detailed guidance relating to the identification and assessment of risks at the financial statement level, and how such risks may affect the assessment of risks at the assertion level.</p> <p>A specific example of this is within Appendix 2 where it introduces the guidance as "The following are examples of events and conditions that may indicate the existence of risks of material misstatement in the financial report, either at the financial statement level or the assertion level" however the subsequent subheading is "Inherent Risk Factors at the Assertion Level".</p> <p>Requirements throughout the standard refer to risks of material misstatement at the assertion level. In many instances, there would also presumably be an impact on financial statement level risks, however the relevant paragraphs refer to the assertion level risks only.</p> <p>We acknowledge that ED 01/18 indicates that financial statement level risks are constituted from assertion level risks with a pervasive impact, however there is no specific guidance on how to determine what assertion level risks constitute financial statement level risks.</p> <p>We recommend that updates are made to include further guidance on financial statement level risks and/or how the auditor should apply the requirements and guidance of the standard to financial statement level risks.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
2	Page 8.	R2	<p>The guidance on how to assess the financial statement level risks is enhanced however the guidance on how to apply the assessment to the risks of material misstatement is lacking in detail. Conceptually based on the risk assessment process described by the revised standard any financial statement level risks such as going concern or management override of controls would already be considered as part of the risk assessment process at the balance or transaction level and therefore other than as a stand back option the assessment of risks at the financial statement level appears to be repetitive, and not enhancing audit quality in of itself.</p>	Inconsistent with feedback from other stakeholders, not included in submission.
3	Page 13.	KPMG	<p>Yes, the guidance better clarifies how risks that affect a number of assertions have a more pervasive effect on the financial statements and therefore need to be assessed to develop overall responses, as</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			well as the consideration of how such risks affect the assessment of risks of material misstatement at the assertion level.	
4	N/A	UNSW	No response provided.	N/A
5	Page 8.	ACAG	ACAG supports the additional guidance material. It clarifies how the control environment can have a pervasive effect on financial reporting and fraud.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 8 – What are your views about the proposed stand-back requirement in paragraph 52 of ED 01/18 and the proposed revisions made to paragraph 18 of ASA 330 and its supporting application material? Should either or both requirements be retained? Why or why not?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Pages 6 & 10-11.	Deloitte	<p>The proposed stand-back requirement promotes the application of professional judgement and professional scepticism, and is an important step of the risk assessment process to prompt the auditor to holistically consider the appropriateness of the risk assessment made.</p> <p>The proposed revision made to paragraph 18 of ASA 330 to specifically articulate that a material class of transaction, account balance and disclosure can be material based on quantitative or qualitative factors is supported, however difficulty in understanding arises from confusion around what constitutes a significant class of transaction, account balance and disclosure versus a material but not significant transaction, account balance and disclosure which we have detailed further in Appendix 2.</p> <p>Linked to our overriding comment above, we highlight that the wording utilised is potentially misleading and confusing due to the reference to 'quantitatively or qualitatively material' and the definition of a significant class of transactions, account balance or disclosure. We question whether it is possible for the auditor to identify a class of transactions, account balance or disclosure that is qualitatively material that has not been identified as significant. Perhaps the reference to a class of transactions, account balance or disclosure that is 'quantitatively material' infers that it is greater than materiality.</p> <p>From our perspective that the purpose of this paragraph is for the auditor to perform a 'sense check' and reassess whether their original conclusions remain true (although this depends on the outcome of our earlier comments relating to significant and material classes of transactions, account balances and disclosures). As a result, we recommend that the wording of paragraph 52(a) be amended to remove reference to 'quantitatively or qualitatively material' so it reads as follows:</p> <p>"The auditor shall: (a) Identify the classes of transactions, account balances and disclosures that have not been identified as significant classes of transactions, account balances or disclosures in accordance with paragraph 46;"</p> <p>Paragraph 52 is supported by guidance paragraphs A240-A242. We believe that the content included within paragraphs A241 and A242 does not provide relevant guidance to the auditor and if anything, creates further confusion and ambiguity.</p> <p>Paragraph A241 indicates that there can be transactions, account balances or disclosures that are quantitatively or qualitatively material but are not determined as significant transactions, account</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>balances or disclosures as there are no relevant assertions, and then provides an example that fails to explain or differentiate.</p> <p>Paragraph A242 incorporates a reference to paragraph 18 of ASA 330 which states "irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure". We are struggling to understand how this links to supporting paragraph 52 of ASA 315.</p>	
2	Page 9	R2	<p>The revised stand back provision is a better and more comprehensive consideration than ASA 330 para 18. Retaining both in separate forms is not an option designed to enhance audit quality or consistency given they address the same concept. The ASA 315 revised wording should be adopted in both standards. Failing this the ASA 315 should be consistent with ASA 330 rather than having a different definition.</p> <p>However, of greater concern is the relevance of the paragraph at all given the definition of reasonable possibility as being remote meaning that in almost all scenarios all balances and all assertions could be considered at risk of material misstatement, rendering any stand back provision essentially redundant. The concept of the stand back provision is very good but only where there is a likelihood of there being balances and transactions which have not been identified as having risks of material misstatement.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
3	Page 14.	KPMG	<p>We do not believe that it is critical that ED 01/18 include a stand back requirement, since there is greater emphasis now on the iterative nature of the risk assessment process, as well as the increased clarity in respect of how and why to perform each step.</p> <p>However, given the complexity of the standard and the fact that many of the steps are performed concurrently, which necessitates the auditor to continually update its understanding and consideration of views formed and assessments made, we believe that overall it may be helpful to have a stand back at the end of the risk assessment process, before the auditor proceeds to the execution of responses.</p> <p>We do not consider it appropriate to retain the stand back at ISA 330.18, as we believe that the placement of this requirement at a relatively advanced stage of the audit, as well as the specific language used ("irrespective of [the risk identification and assessment procedures performed]") may serve to reduce the emphasis on the risk identification and assessment process as a critical part of the audit process.</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
4	N/A	UNSW	No response provided.	N/A
5	Pages 8-9.	ACAG	<p>ACAG generally supports stand back provisions however it is unclear the benefit of this particular provision. Unlike the stand back provision in the proposed ASA 540 <i>Auditing Accounting Estimates and Related Disclosures</i>, this procedure appears unlikely to result in a meaningful improvement to audit quality because it simply requires the auditor to double-check the completeness of risks with respect to material balances. In our view the auditor, in conducting risk assessment procedures to understand the entity, its environment and financial reporting framework, should already have considered material transactions, balances and disclosures in identifying sources of risk. The application of appropriate levels of skills and experience (including engagement leader review) consistent with ASA 220 <i>Quality Control for an Audit of a Financial Report and Other Historical Financial Information</i> is more effective than this stand back requirement in improving the quality of risk assessments.</p> <p>ACAG believes that the requirements in ASA 330 should be retained because it will continue to enhance the application of qualitative considerations to financial reporting.</p>	Inconsistent with feedback from other stakeholders. Mixed views have been included in submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 9 – Effective date: the IAASB have proposed that the standard will be effective for financial reporting periods commencing on or after 15 December 2020, which is anticipated to be approximately 18 months after approval of the final ISA. Do you think this is a sufficient period to support effective implementation of the new standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 6.	Deloitte	This appears to be a sufficient timeframe, however we note that amendments are also proposed for ASA 200, 240 and 330 to support changes within ASA 315. Given ED 01/18 permits early adoption prior to 15 December 2020, effective implementation of the ASA 315 will be contingent on the adoption of the suite of changes (that include those in ASA 200, 240 and 330) and thus we believe this should be clearly stated in the new/updated standards.	AUASB has previously deliberated on this matter and agreed with the proposed IAASB implementation date for ISA 315 of December 2020. No stakeholders raised significant concerns with the application date. The AUASB Submission reflects this.
2	Page 9.	R2	It is not possible to comment on the sufficiency of time to implement this at this time, the changes required to software and methodology may take longer to implement than the allotted time. We certainly would not support any earlier release of the revised standard as the impact of the changes in documentation and the structure of risk assessment will require considerable work.	AUASB has previously deliberated on this matter and agreed with the proposed IAASB implementation date for ISA 315 of December 2020. No stakeholders raised significant concerns with the application date. The AUASB Submission reflects this.
3	Page 14.	KPMG	We do not have any other specific comments in respect of the questions posed. We believe the effective date to be a reasonable implementation period.	AUASB has previously deliberated on this matter and agreed with the proposed IAASB implementation date for ISA 315 of December 2020. No stakeholders raised significant concerns with the application date. The AUASB Submission reflects this.
4	N/A	UNSW	No response provided.	N/A
5	Page 9.	ACAG	ACAG considers ASA 315 to be a fundamental auditing standard that warrants significant consultation and debate prior to approval. ACAG considers the 18-month post approval period to be sufficient timing to support effective implementation.	AUASB has previously deliberated on this matter and agreed with the proposed IAASB implementation date for ISA 315 of December 2020. No stakeholders raised significant concerns with the

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
				application date. The AUASB Submission reflects this.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 10 – Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 6.	Deloitte	Nothing further to note.	N/A
2	Page 9.	R2	None noted.	N/A
3	Page 14.	KPMG	We believe the applicable laws and regulations have been appropriately addressed and no references to relevant laws or regulations have been omitted.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 10	ACAG	<p>ACAG considers the public sector guidance to be of marginal help, the standard would be strengthened by further guidance with respect to:</p> <ul style="list-style-type: none"> - interaction between this standard and additional Auditor-General responsibilities arising out of legislative mandates and Auditor-General audit standards; - the influences of Parliament and the Executive, such as the directions of Shareholding Ministers; - impact or influence of Machinery of Government changes; - explicit statement of the requirements to audit probity and propriety risks. 	To be considered as part of Australian modifications to the standard. Not included in the AUASB submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 11 – Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 6.	Deloitte	Nothing further to note.	N/A
2	Page 9.	R2	None noted.	N/A
3	Page 14	KPMG	We do not believe any applicable laws and regulations may impact or conflict with the proposed standard.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 10.	ACAG	ACAG is not aware of any such laws and regulations.	N/A
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 12 – Whether there are any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 6.	Deloitte	None noted.	N/A
2	Page 9.	R2	None noted.	N/A
3	Page 14.	KPMG	We are not aware of any principles and practices that may impact the application of or conflict with the proposed standard.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 10.	ACAG	A well-informed risk assessment is critical to audit quality. ACAG has not identified any principles and practices that would compromise audit quality.	N/A
6	Pages 1-3.	IIA	<p>To the first part of this question, IIA-Australia believes that there are current internal audit principles and practices that should be acknowledged in this revised standard, which would enhance and improve the application of ASA 315.</p> <p>We believe a critical change would enable external auditors to confidently exercise professional skepticism in identifying and assessing the risks of material misstatement, particularly in relation to internal controls and in their dealings with the internal audit function. Paragraph A19 states “Regardless of the source of information, the auditor considers the relevance and reliability of the information to be used as audit evidence in accordance with ASA 500”.</p> <p>As you would be aware, ASA 500 Audit Evidence is considered by the auditor when assessing the relevance and reliability of the information to be used. Paragraph 7 of ASA 500 states in part “the auditor shall consider the relevance and reliability of the information to be used as audit evidence.” Paragraph 8 goes on to say “If information to be used as audit evidence has been prepared using the work of a management expert, the auditor shall, to the extent necessary, having regard to the significance of that expert’s work for the auditor’s purposes: (a) Evaluate the competence, capabilities and objectivity of that expert”</p>	<p>ISA/ASA 610 <i>Using the Work of Internal Auditors</i> already deals extensively with the Auditors’ requirement to assess the adequacy of the work of the internal audit function and is explicitly referenced via footnote in Paragraph 34 of the ISA 315 ED, as well as a number of related paragraphs in the application material.</p> <p>The ATG considers that the ASA 315 ED addresses how the knowledge and experience of the internal audit function informs the external auditor’s understanding of the entity and its environment and identification and assessment of risks of material misstatement. The ED also explains how effective communication between</p>

Item No.	Ref Page No.	Respondent Comment	ATG Commentary
		<p>IIA-Australia contends that, for consistency with ASA 500, ASA 315 could be improved by having the external auditor satisfy him or herself that the internal auditor that they are dealing with is competent, capable and objective.</p> <p>IIA-Australia believes that guidance is needed to enable the auditor to form a proper judgement. This can be achieved by the auditor asking a threshold question: “Has the work performed by the internal audit function conformed to the International Internal Auditing Standards contained in The IIA’s International Professional Practices Framework?”</p> <p>Conformance with the International Internal Audit Standards indicates that the internal audit function is competent, capable and objective. If an internal audit function cannot provide this assurance, then the ability to rely on the work of that internal audit function should be open to question and doubt.</p> <p>Our key message here is that you can rely on the work of internal auditors if they conform to the International Internal Audit Standards as issued, from time to time, by the International Internal Audit Standards Board.</p> <p>In Exposure Draft 315, paragraph A28 states “Appropriate individuals within the internal audit function with whom enquiries are made are those who, in the auditor’s judgement, have the appropriate knowledge, experience and authority, such as the chief audit executive or, depending on the circumstances, other personnel within the function.”</p> <p>Exposure Draft 315 does not provide guidance for the auditor to evaluate whether an internal auditor is knowledgeable and how the work was performed. Currently it is left entirely to the auditor to form a judgement about, the internal audit function, and with which he or she is unlikely to be familiar. IIA-Australia maintains that this is a fundamental weakness that should be addressed in the Exposure Draft.</p> <p>We believe that all internal audit practitioners should be knowledgeable about their trade. Knowledge can be demonstrated by the head of the internal audit function, or someone they have access to, if they have successfully completed and hold the Certified Internal Auditor® designation, or the Australian Graduate Certificate in Internal Auditing qualification, or having been made a Professional Member of the Institute Internal Auditors – Australia (PMIIA). IIA-Australia believes this should be written into the revised ASA 315, or at the very least footnoted.</p> <p>In summary, IIA-Australia believes that audit quality can be improved in Australia by having the auditor satisfy him or herself that the internal auditor that they are dealing with is competent, capable and objective (in accordance with ASA 500). To this end, the following wording should be added as follows:</p> <ul style="list-style-type: none"> - Add to the end of paragraph A19: “In respect of the internal audit function, conformance with the International Internal Audit Standards indicates that the internal audit function is competent, 	<p>the internal and external auditors also creates an environment in which the external auditor can be informed of significant matters that may affect the external auditor’s work.</p> <p>ISA/ASA 610 already includes application guidance to assist the external auditor determine the extent to which the internal audit function’s organisational status and relevant policies and procedures support the objectivity and competence of the internal auditors.</p> <p>Accordingly the ATG believe this point does not need to be addressed in the AUASB’s submission.</p>

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
			<p>capable and objective. If an internal audit function cannot provide this assurance, then the ability to rely on the work of that internal audit function should be open to question and doubt.”</p> <p>IIA-Australia believes that Proposed Auditing Standard ASA 315 Identifying and Assessing the Risks of Material Misstatement can be improved with the addition of the following:</p> <ul style="list-style-type: none"> - Paragraph A28: Add after the first sentence “Knowledge can be demonstrated by the head of the internal audit function, or someone they have access to, if they have successfully completed and currently hold the Certified Internal Auditor® designation, or the Australian Graduate Certificate in Internal Auditing qualification, or having been made a Professional Member of the Institute Internal Auditors – Australia (PMIIA).” 	
7	Page 1.	R7	<p>We note that there may be need for an Australian amendment in relation to the reference to internal audit in paragraph 34 in order to ensure that auditors do not breach the requirement in ASA 610 (para) Aus 25.1.</p>	<p>To be considered when adopting the standard as a legislative instrument in Australia.</p>

Question 13 – What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

Qn. 13(a) – Where those costs are likely to occur?

Qn. 13(b) – The estimated extent of costs, in percentage terms (relative to audit fee)?

Qn. 13(c) – Whether expected costs outweigh the benefits to the users of audit services?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 7.	Deloitte	<p>The requirements of ED 01/18 appear to enhance requirements compared to the extant ASA 315. The largest compliance impact is likely to be on small and less complex entities, however scalability has been considered within ED 01/18.</p> <p>We do not believe that there will be additional costs arising from the changes to the proposed standard. More risks may be identified with the introduction of new defined concepts, and thus in a market where audit fees are under pressure and are seen as a compliance cost will create challenges on its own, however this will depend on the extent and quality of current audit engagement documentation.</p>	To be considered when adopting the standard as a legislative instrument in Australia.
2	Page 10.	R2	<p>The proposed changes and increased granularity of risk assessment will lead to increased costs across all engagements. The identification of more risks will likely lead to further work again increasing costs. Whether this will result in higher quality audits or reductions in audit failure is unclear at this time. Whether users will consider increased costs of an audit to be a benefit will be determined by the users at a future date.</p>	To be considered when adopting the standard as a legislative instrument in Australia.
3	Page 15.	KPMG	<p>We expect to incur costs associated with training and coaching auditors to apply the changes in requirements. It is difficult to estimate the extent of costs or the proportion of audit fee, as each audit will be impacted in a different manner depending on its size and complexity. We consider that the increase in costs will generally benefit audit quality and therefore the users of audit services.</p> <p>However, we note that incremental costs may be incurred where the auditor is required to comply with the documentation requirement in paragraph 54(d) relating to the rationale for the significant judgements made in identifying and assessing the risks of material misstatement. We expect that the more extensive documentation requirement in paragraph 54(d) of the ED will increase the time spent on documentation, particularly for smaller firms, without an associated benefit for users of audit services.</p>	To be considered when adopting the standard as a legislative instrument in Australia.

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
4	N/A	UNSW	No response provided.	N/A
5	Page 11.	ACAG	ACAG believes some of the adopted terminology may impact scalability and could lead to increased audit costs with little value to the audit process. Examples of this terminology are the concepts of “More than remote” and “small and less complex” rather than “small or less complex”.	To be considered when adopting the standard as a legislative instrument in Australia.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 14 – What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 315 (specific questions/examples would be helpful)?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 7.	Deloitte	Refer to comments raised in response to the above question.	N/A
2	Page 10.	R2	The inclusion of the IAASB flow charts in the standard as appendices.	Included in submission.
3	Page 15.	KPMG	Considering the current status of the ISA 315 project, we cannot at this time identify specific implementation guidance that we would like the AUASB to issue in conjunction with the release of ASA 315.	Noted.
4	N/A	UNSW	No response provided.	N/A
5	Page 11.	ACAG	ACAG would like further consideration of more advanced data analytic techniques to be considered. For example, the use of predictive analytics as a tool for determining risk and additional guidance on the implications of using population data in assessing risk and determining the audit approach.	Included in submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 15 – Are there any other significant public interest matters that stakeholders wish to raise?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 7.	Deloitte	Nothing further to note.	N/A
2	Page 10.	R2	None noted.	N/A
3	Page 15.	KPMG	No, there are no other significant public interest matters that we wish to raise.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 11.	ACAG	ACAG is not aware of any other significant public interest matters.	N/A
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

EXHIBIT 2: Comments related to ED 02/18– Proposed Auditing Standard ASA 2018-1 – *Amendments to Australian Auditing Standards*

Question 1 – With respect to the proposed conforming and consequential amendments to:

Qn. 1(a) – ASA 200 (including Appendix 2), ASA 240 and ED 03/18, are these appropriate to reflect the corresponding changes made in proposed ASA 315?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 12.	R2	None comments.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 9.	ACAG	ACAG considers the proposed conforming and consequential amendment to ASA 200, ASA 240, ED 03/18 and ASA 330 are appropriate. We would like further considerations to consistency of application for ASA 402, 600 and 620.	The ATG notes that ISA 600 due to be revised in 2019, any required consequential amendments arising from the revision of ASA/ISA 315 will be considered as part of this project. The point in respect of ASA 402 and ASA 620 will be included in other matters raised in the AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 1(b) – ASA 330, are the changes appropriate in light of the enhancements that have been made in proposed ASA 315, in particular as a consequence of the introduction of the concept of general IT controls relevant to the audit?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 12.	R2	No comments.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 9.	ACAG	ACAG considers the proposed conforming and consequential amendment to ASA 200, ASA 240, ED 03/18 and ASA 330 are appropriate. We would like further considerations to consistency of application for ASA 402, 600 and 620.	The ATG notes that ISA 600 due to be revised in 2019, any required consequential amendments arising from the revision of ASA/ISA 315 will be considered as part of this project. The point in respect of ASA 402 and ASA 620 will be included in other matters raised in the AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Qn. 1(c) – The other ASAs as presented in Appendix 1, are these appropriate and complete?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 12.	R2	Yes.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 9.	ACAG	ACAG considers the proposed conforming and consequential amendment to ASA 200, ASA 240, ED 03/18 and ASA 330 are appropriate. We would like further considerations to consistency of application for ASA 402, 600 and 620.	The ATG notes that ISA 600 due to be revised in 2019, any required consequential amendments arising from the revision of ASA/ISA 315 will be considered as part of this project. The point in respect of ASA 402 and ASA 620 will be included in other matters raised in the AUASB Submission.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 2 – Do you support the proposed revisions to paragraph 18 of ASA 330 to apply to classes of transactions, account balances or disclosures that are “quantitatively and qualitatively material” to align with the scope of the proposed stand-back in proposed ASA 315?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 12	R2	The proposed change to ASA 330 para 18 is not consistent with the stand back para in the proposed ASA 315. As mentioned in the submission on ED 1, the wording in the proposed ASA 315 is preferable. Failing that at a minimum ASA 315 and ASA 330 should be consistent in their phrasing.	This is consistent with feedback from a range of stakeholders. Included in AUASB Submission.
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 9.	ACAG	Subject to the clarification of our concern raised in question 6d) above, ACAG supports this.	
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 3 – Effective Date: the IAASB have proposed that the standard will be effective for financial reporting periods commencing on or after 15 December 2020, which is anticipated to be approximately 18 months after approval of the final ISA 315. Do you think this is sufficient period to support effective implementation of the new standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 12	R2	We cannot comment on whether this is sufficient time as this will be dependent on external factors such as software providers, however, under no circumstances would less time be appropriate.	AUASB has previously deliberated on this matter and agreed with the proposed IAASB implementation date for ISA 315 of December 2020. No stakeholders raised significant concerns with the application date. The AUASB Submission reflects this.
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 10.	ACAG	ACAG considers the 18-month post approval period to be sufficient timing to support effective implementation.	AUASB has previously deliberated on this matter and agreed with the proposed IAASB implementation date for ISA 315 of December 2020. No stakeholders raised significant concerns with the application date. The AUASB Submission reflects this.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 4 – Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 13	R2	None noted.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 9.	ACAG	<p>ACAG considers the public sector guidance to be of marginal help, the standard would be strengthened by further guidance with respect to:</p> <ul style="list-style-type: none"> - interaction between this standard and additional Auditor-General responsibilities arising out of legislative mandates and Auditor-General audit standards; - the influences of Parliament and the Executive, such as the directions of Shareholding Ministers; - impact or influence of Machinery of Government changes; - explicit statement of the requirements to audit probity and propriety risks. 	
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 5 – Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 13	R2	None noted.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 10.	ACAG	ACAG is not aware of any such laws and regulations.	N/A
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 6 – Whether there are any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 13	R2	None noted.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 10.	ACAG	A well-informed risk assessment is critical to audit quality. ACAG has not identified any principles and practices that would compromise audit quality.	N/A
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 7 – What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

Qn. 7(a) – Where those costs are likely to occur;

Qn. 7(b) – The estimated extent of costs, in percentage terms (relative to audit fee); and

Qn. 7(c) Whether expected costs outweigh the benefits to the users of audit services?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 13.	R2	<p>(a) The increased granularity of risk assessment in the proposed ASA 315 will lead to increased planning time and most likely increased fieldwork time as more risks is likely to result in an increased level of work. Without having performed some engagements under the proposed standard the areas where these costs will occur is not certain.</p> <p>(b) Without having performed engagements under the proposed standard the extent of the increase in costs is not possible to estimate accurately.</p> <p>(c) It is not possible to determine whether increased granularity of risk assessment will be considered to be of additional benefit to the users of the accounts when offset by the increased costs.</p>	To be considered when adopting the standard as a legislative instrument in Australia.
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 11.	ACAG	ACAG believes some of the adopted terminology may impact scalability and could lead to increased audit costs with little value to the audit process. Examples of this terminology are the concepts of “More than remote” and “small and less complex” rather than “small or less complex”.	To be considered when adopting the standard as a legislative instrument in Australia.
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

Question 8 – Are there any other significant public interest matters that stakeholders wish to raise?

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	N/A	Deloitte	No response provided.	N/A
2	Page 13.	R2	None noted.	N/A
3	N/A	KPMG	No response provided.	N/A
4	N/A	UNSW	No response provided.	N/A
5	Page 11.	ACAG	ACAG is not aware of any other significant public interest matters.	N/A
6	N/A	IIA	No response provided.	N/A
7	N/A	R7	No response provided.	N/A

EXHIBIT 3: Other comments on ED 01/18 & ED 02/18

Item No.	Ref Page No.	Respondent Comment		ATG Commentary
1	Page 12.	Deloitte	<p>As previously mentioned (refer to our response to question 3 in Appendix 1), ED 01/18 should be updated to articulate the expectations and requirements over information prepared by the entity used for risk assessment purposes.</p> <p>Further guidance is needed on what constitutes information produced by the entity that is used for risk assessment purposes, and what the expectations and requirements are in relation to understanding and/or obtaining evidence over the reliability of this information (including the nature, timing and extent of testing).</p>	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
2	Page 12.	Deloitte	Paras. 5 and 48 – These paragraphs make reference to assessing risk based on the magnitude of misstatement, however our view is that the wording should be aligned to the wording in paragraphs A10 and A222 which reference the "potential magnitude" of the misstatement were that misstatement to occur, and "magnitude of the possible misstatement".	Inconsistent with feedback from other stakeholders. Not included in AUASB Submission.
3	Page 12.	Deloitte	Para 6. – We note a repeated comma in the final sentence of this paragraph.	Noted for editorial.
4	Page 12.	Deloitte	<p>54 - We note that this paragraph relating to audit documentation does not have an overarching requirement to indicate that auditors need to use professional judgement in the documentation of the procedures they have performed as part of the risk assessment. The current wording of this paragraph promotes a risk that auditors will interpret paragraph 54 to mean that only the items stipulated require documentation.</p> <p>This paragraph also does not include a requirement to document key considerations and judgements, such as those relating to the stand-back requirement in paragraph 10, nor control deficiencies identified in paragraph 43 or risk assessment procedures performed in paragraph 17.</p> <p>We recommend that an overarching paragraph indicating the requirement to utilise professional judgement be included at the start of this paragraph.</p>	Consistent with feedback received from other stakeholders. Included as an "Other Matter" in AUASB Submission.
5	Pages 10-11	R2	Para. A10 – The guidance in Para A10 is repetitive and does not actually provides guidance. Sentence 2 repeats, 1, as does 3. And ultimately it says matters are significant because of how much work you do, but how do you know how much work to do because it's a significant risk, the whole thing seems circular, compared to the previous 6 factors of a significant risk in the extant standard, which suggested where the significant risks would lie.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.

6	Page 11	R2	Para. 17(c) – This para is inconsistent with the use of the words "audit evidence" in question 4 above.	Consistent with feedback received from other stakeholders. Included in AUASB Submission.
7	Page 11	R2	Para. 54(a) – What is a significant decision? Likely additional documentation requirements in planning, but no substantive guidance on what specifically constitutes a significant decision is included in the standard.	Inconsistent with feedback from other stakeholders. Not included in AUASB Submission.
8	Page 11	R2	Para. A146 – Missing “of”?	Editorial.

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The Chairman
Australian Auditing and Assurance Standards Board
PO Box 204, Collins Street West
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3 October 2018

Dear Chairman

Re: Exposure Draft ED 01/18 – *Proposed Auditing Standard ASA 315 Identifying and Assessing the Risks of Material Misstatement*

Deloitte Touche Tohmatsu (Deloitte) is pleased to respond to the Australian Auditing and Assurance Standards Board's (AUASB) Exposure Draft ED 01/18 – Proposed Auditing Standard ASA 315 *Identifying and Assessing the Risks of Material Misstatement* ("ED 01/18").

Overall we support having one set of international standards on auditing that are used by practitioners worldwide in the audit of a financial report (although we also acknowledge that there may be certain circumstances where compelling reasons exist for the inclusion of Australian specific requirements and guidance). Based on the specific comments on ED 01/18 included within Appendices 1 and 2 relating to fundamental concepts and definitions, we are of the view that further consideration is required prior to the issuance of ASA 315, otherwise there is a risk of misunderstanding and incorrect application of the standard.

Please refer to Appendix 1 for our responses to the specific questions posed by the AUASB within ED 01/18.

In addition, we have included comments relating to specific concepts and definitions within the proposed auditing standard in Appendix 2.

If you have any queries in relation to this response please do not hesitate to contact me on 02 9322 3434.

Yours sincerely



Gareth Bird
Partner
Deloitte Touche Tohmatsu

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Appendix 1 – Response to specific questions posed within ED 01/18

1. *Has ED 01/18 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risks of material misstatement. In particular:*

(a) Do the proposed changes help with the understandability of the risk identification and assessment process?

Overall we believe the changes to ED 01/18 are improvements to the previous version of the standard, however there does remain a number of areas that may cause misunderstanding or confusion (for example, the concept of a significant class of transactions, account balance or disclosure versus a material class of transactions, account balance or disclosure; inherent risk versus control risk and the consideration of controls when identifying and assessing risks of material misstatement), which need to be addressed prior to the revisions, promoting a robust risk identification and assessment process.

The complexity and professional judgement required when identifying and assessing the risks of material misstatement, as well as the sheer volume of the standard also create potential application challenges relating to consistency and robustness.

Please refer to our detailed responses below and within Appendix 2.

(b) Are the flowcharts, prepared by the IAASB, helpful in understanding the flow of the standard (i.e., how the requirements interact and how they are iterative in nature)? If yes, should they be included in the final Standard?

We understand that the flowcharts are aimed to add value, however we also acknowledge that due to the complexity and iterative nature of risk assessment, the flowcharts do require careful consideration and are not “quick reference guides”. There are some challenges with the ordering and sequencing of certain steps (for example, relating to the identification of material but not significant classes of transactions, account balances and disclosures after identifying and assessing the significant classes of transactions, account balances and disclosures) within the flowcharts.

If flowcharts are included in the final standard, it is important that they clearly present what is inherently an iterative process and where multiple steps are concurrently occurring.

(c) Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6–28 of the IAASB’s Explanatory Memorandum.

Yes, however we believe there are a number of inconsistencies and areas needing clarification relating to key concepts and terminology that need to be addressed. Refer to our response to question 1(a) above, as well as Appendix 2.

(d) Are the new introductory paragraphs helpful?

We consider the introductory paragraphs to be too detailed in the context of their purpose as an introduction. As a consequence of this detail they:

- attempt to introduce multiple concepts which causes duplication in the standard
- may be interpreted by practitioners as setting requirements that should be specifically addressed in addition to those within the body of the standard
- create potential confusion about the requirement to understand the entity and environment, including the system of internal control that forms the basis of the identification of risks of misstatement versus the identification of inherent risk before consideration of any related controls
- refer to risks at the assertion level only (from paragraph 4 onwards) and do not refer to financial statement level risks.

2. *Are the requirements and application material of ED 01/18 sufficiently scalable, including the ability to apply ED 01/18 to the audits of entities with a wide range of sizes, complexities and circumstances?*

Yes, we note that paragraph A16 indicates: “the auditor’s risk assessment procedures to obtain the overall understanding may be less extensive in audits of smaller and less complex entity”, and that this has been followed by references to differing requirements for “smaller and less complex” entities in various other paragraphs, as has been highlighted in the IAASB’s Explanatory Memorandum. However, the length of the standard may possibly create a challenge in applying this to a very small entity.

3. *Do stakeholders agree with the approach taken to enhancing ED 01/18 in relation to automated tools and techniques, including data analytics, through the use of examples to illustrate how these are used in an audit (see Appendix 1 of the IAASB’s Explanatory Memorandum for references to the relevant paragraphs in ED 01/18)? Are there other areas within ED 01/18 where further guidance is needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?*

Yes, we agree with the enhancement of ED 01/18 in relation to references to automated tools and techniques, particularly within paragraphs A17-A19, A33 and A48

Another area where further guidance is needed is in relation to the underlying data used within the automated tools and techniques when this constitutes information produced by the entity that is used for risk assessment procedure purposes, and what the requirements are in relation to understanding and/or obtaining evidence over the reliability of this information (including the nature, timing and extent of testing).

4. *Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk identification and assessment process? Do you support the proposed change for the auditor to obtain ‘sufficient appropriate audit evidence’ through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional scepticism?*

In our view ED 01/18 somewhat supports the appropriate exercise of professional scepticism by the inclusion of references to where professional scepticism may be considered or is encouraged, such as within paragraphs A44, A47 and A201.

In our view, more explicit references to the expectation and requirement to exercise professional scepticism could be included within the standard, and this could include guidance on the types of procedures to perform, and the associated documentation requirements.

We support the proposed change for the auditor to obtain “sufficient appropriate audit evidence” through the performance of risk assessment procedures, however we note that paragraph 54 does not require the auditor to document the procedures performed as part of paragraph 17. It is our view that a requirement to document the procedures performed be included within paragraph 54.

5. *Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks or material misstatement? Specifically:*

(a) Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?

Yes, the additional guidance in the latest exposure draft enhances the understanding of what is required of the auditor in documenting the components of the entity’s system of internal control. Additionally the updated definitions provide greater relevancy and clarity.

(b) Have the requirements related to the auditor's identification of controls relevant to the audit been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?

Paragraph 39 and the associated guidance paragraphs have enhanced the standard, however we don't believe that they have provided a lot of clarity on what constitutes other controls relevant to the audit, and the expectations and requirements on how the auditor determines these. We acknowledge there is some enhanced guidance within paragraph A179 however this doesn't extend to providing clarity on how the auditor may go about determining what other controls are relevant in the circumstances.

Similarly, paragraph A167 indicates that for smaller and less complex entities, there may not be any other controls aside from the minimum expectation of controls over journal entries, however does not provide guidance on how the auditor should exercise professional judgement in making this determination. It also doesn't contemplate the common situation for smaller and less complex entities where controls exist but are not formally documented.

(c) Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor's understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor's consideration of the effects of the entity's use of IT on the identification and assessment of the risks of material misstatement?

Yes, we support the introduction of the new IT-related concepts and definitions as they provide a baseline understanding for auditors.

The enhanced requirements and application materials around the impact of the IT environment and IT controls on the identification and assessment of risks of material misstatement is useful in assisting the auditor to understand the various elements of what is required as part of the risk assessment process.

Having said this, we highlight that it is a requirement under paragraph 38 that the auditor obtains an understanding of the control activities component - how this interacts with risk identification and assessment is unclear particularly in the context where the identification of risks of misstatement is made before the consideration of controls (refer to our response to question 1(a) and our comments in Appendix 2).

6. *Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:*

(a) Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments'?

Yes, we support the separate assessments of inherent and control risk to the extent of preventing auditors from "taking credit for controls" when determining risks of material misstatement, however we believe that there is a need to clearly articulate the consideration of controls when assessing inherent risk (that is, using the understanding of the control environment and internal controls that exist) and what is included within the assessment of inherent risk versus control risk (for example, where the entity does not have an appropriate control or the control is not designed or implemented appropriately, whether this is incorporated as part of the inherent risk or control risk assessment).

Furthermore, in the introduction paragraphs it states that the assessment of the risks of material misstatement at the assertion level are based on the separate assessments of inherent risk and control risk, however there is no clarity or guidance on how the combination of these separate assessments come together when determining the risk of material misstatement. Following on from this, it is highlighted that control risk would be assessed at "maximum" if the auditor does not intend to rely on the operating effectiveness of control(s) that address the risk of material misstatement, however there is no linkage or connection to the understanding of the control environment and the

design and implementation of these controls (which we assume is part of the inherent risk assessment, although this is not directly stated).

Refer to our detailed comments within Appendix 2.

(b) Do you support the introduction of the concepts and definitions of 'inherent risk factors' to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor's risk assessment process?

Yes, we support the introduction of these concepts and definitions, however we note that whilst the factors have been established, they are quite high level and how the auditor applies these factors against a spectrum of risk assessment has not been explained, nor guidance provided.

(c) In your view, will the introduction of the 'spectrum of inherent risk' (and the related concepts of assessing the likelihood of occurrence, and magnitude, of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?

This formalises a concept that auditors have already been utilising, however more guidance is needed in the application of professional judgement if consistency in the identification and assessment of the risks of material misstatement and significant risk is to be achieved, as currently the implementation guidance only indicates what to look for, rather than how to assess. The term "spectrum" itself has not been defined, nor is guidance included.

In addition, there does not appear to be a similar spectrum concept for the control risk assessment - the standard describes only "maximum" and "less than maximum". These options are not clearly defined either, and application guidance is not included.

Magnitude is a new way of thinking and can be misinterpreted without specific guidance. Auditors are used to "material" and "significant" and thus magnitude needs to be defined.

(d) Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e., an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion), and how they assist the auditor in identifying where risks of material misstatement exist?

Please refer to our detailed comments within Appendix 2 of this response.

(e) Do you support the revised definition, and related material, on the determination of 'significant risks'? What are your views on the matters presented in paragraph 57 of the IAASB's Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?

Yes, the previous definition of significant risks within the extant ISA 315 focused on the response to a significant risk, rather than defining what a significant risk is. Whilst we agree with defining significant risks as relating to inherent risk close to the upper end of the risk spectrum, we highlight the fact that this does not consider situations where significant risk may arise due to inherent risk being exacerbated by issues with internal controls. In addition, linking to our response to question 6(b) above, the risk spectrum is not defined and no further guidance is included to assist in understanding the concept of the "upper end" of the spectrum.

7. *Do you support the additional guidance in relation to the auditor's assessment of risks of misstatement at the financial statement level, including the determination about how, and the degree to which, such risks may affect the assessment of risks at the assertion level?*

We support the need for additional guidance in relation to the auditor's assessment of risks of misstatement at the financial statement level. We note however that the guidance within ED 01/18 is largely centred on the risk of misstatement at the assertion level. ED 01/18 does not contain detailed guidance relating to the identification and assessment of risks at the financial statement level, and how such risks may affect the assessment of risks at the assertion level.

A specific example of this is within Appendix 2 where it introduces the guidance as "The following are examples of events and conditions that may indicate the existence of risks of material misstatement in the financial report, either at the financial statement level or the assertion level" however the subsequent subheading is "Inherent Risk Factors at the Assertion Level".

Please refer to additional comments relating to the assessment of risks of misstatement at the financial statement level within our detailed comments in Appendix 2.

8. *What are your views about the proposed stand-back requirement in paragraph 52 of ED 01/18 and the proposed revisions made to paragraph 18 of ASA 330 and its supporting application material? Should either or both requirements be retained? Why or why not?*

The proposed stand-back requirement promotes the application of professional judgement and professional scepticism, and is an important step of the risk assessment process to prompt the auditor to holistically consider the appropriateness of the risk assessment made.

The proposed revision made to paragraph 18 of ASA 330 to specifically articulate that a material class of transaction, account balance and disclosure can be material based on quantitative or qualitative factors is supported, however difficulty in understanding arises from confusion around what constitutes a significant class of transaction, account balance and disclosure versus a material but not significant transaction, account balance and disclosure which we have detailed further in Appendix 2.

9. *Effective date: the IAASB have proposed that the standard will be effective for financial reporting periods commencing no or after 15 December 2020, which is anticipated to be approximately 18 months after approval of the final ISA. Do you think this is a sufficient period to support effective implementation of the new standard?*

This appears to be a sufficient timeframe, however we note that amendments are also proposed for ASA 200, 240 and 330 to support changes within ASA 315. Given ED 01/18 permits early adoption prior to 15 December 2020, effective implementation of the ASA 315 will be contingent on the adoption of the suite of changes (that include those in ASA 200, 240 and 330) and thus we believe this should be clearly stated in the new/updated standards.

10. *Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?*

Nothing further to note.

11. *Whether there are any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?*

None noted.

12. *Whether there are any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?*

None noted.

13. *What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:*

- (a) Where those costs are likely to occur;*
- (b) The estimated extent of costs, in percentage terms (relative to audit fee); and*
- (c) Whether expected costs outweigh the benefits to the users of audit services?*

The requirements of ED 01/18 appear to enhance requirements compared to the extant ASA 315. The largest compliance impact is likely to be on small and less complex entities, however scalability has been considered within ED 01/18.

We do believe that there will be additional costs arising from the changes to the proposed standard. More risks may be identified with the introduction of new defined concepts, and thus in a market where audit fees are under pressure and are seen as a compliance cost will create challenges on its own, however this will depend on the extent and quality of current audit engagement documentation.

14. *What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 315 (specific questions/examples would be helpful)?*

Refer to comments raised in response to the questions above.

15. *Are there any other significant public interest matters that stakeholders wish to raise?*

Nothing further to note.

Appendix 2 – Other specific comments relating to proposed changes within ED 01/18

ED 01/18 Paragraph	Comment
Amendments to ED 01/18	
Overriding	<p>We question why the introduction of a new concept 'significant class of transactions, account balance or disclosure' is required and how it differs from a material class of transactions, account balance or disclosure referred to in ASA 330.</p> <p>Paragraph 4 states: <i>"the assertions to which such risks of material misstatement relate are referred to as 'relevant assertions,' and the classes of transactions, account balances and disclosures to which the relevant assertions relate are referred to as 'significant classes of transactions, account balances and disclosures.'"</i></p> <p>Intuitively we would equate a significant class of transactions, account balance or disclosure to be the same as a material class of transactions, account balance or disclosure as fundamentally it comes down to the existence of one or more risks of material misstatement associated with one or more relevant assertions, however this is not how it is currently structured.</p> <p>Paragraph 10 indicates that: <u>"After identifying the risks of material misstatement, the auditor determines the significant classes of transactions, account balances and disclosures. The auditor is also required to perform a stand-back to confirm that this identification is appropriate."</u></p> <p>Similarly paragraph 46 requires that: <u>"The auditor shall determine significant classes of transactions, account balances and disclosures, and their relevant assertions, based on the identified risks of material misstatement."</u></p> <p>It appears that a significant class of transactions, account balance or disclosure is a subset of a material class of transactions, account balance or disclosure (i.e. a significant class of transactions, account balance or disclosure is always a material class of transactions, account balance or disclosure, but not vice versa), but this is not clearly defined and the concepts/definitions are not currently articulated to distinguish between them.</p> <p>The inclusion of a significant class of transactions, account balance or disclosure within ASA 315 is misleading and confusing as there is no clear distinction between this and a material class of transactions, account balance or disclosure.</p> <p>As a consequence, it is unclear what the expectation of the auditor is under Paragraph 10 and 46.</p> <p>Refer also to our comment below on paragraphs 52 and A240-A242.</p>
Overriding	<p>Requirements throughout the standard refer to risks of material misstatement at the assertion level. In many instances, there would also presumably be an impact on financial statement level risks, however the relevant paragraphs refer to the assertion level risks only.</p>

	<p>We acknowledge that ED 01/18 indicates that financial statement level risks are constituted from assertion level risks with a pervasive impact, however there is no specific guidance on how to determine what assertion level risks constitute financial statement level risks.</p> <p>We recommend that updates are made to include further guidance on financial statement level risks and/or how the auditor should apply the requirements and guidance of the standard to financial statement level risks.</p>
4, 5, 39(e)	<p>We note that different paragraphs convolute the consideration of the entity's controls with respect to the identification and assessment of risks of material misstatement. Some of these paragraphs are included within the "Key Concepts in this ASA" section, so they are critical for auditors to understand when applying the standard.</p> <p>Within paragraph 4, it states "<u>The required understanding of the entity and the environment, the applicable financial reporting framework, and the system of internal control forms the basis for the auditor's identification of risks of material misstatement. The identification of risks of material misstatement at the assertion level is performed before consideration of any controls.</u>"</p> <p>Paragraph 39(e) states: <i>[The auditor shall identify controls relevant to the audit, being those:] That, in the auditor's professional judgement, are appropriate to evaluate their design and determine whether they have been implemented to enable the auditor to:</i> <i>(i) Identify and assess the risks of material misstatement at the assertion level; or</i> <i>(ii) Design further audit procedures responsive to assessed risks.</i></p> <p>The "Identifying and Assessing the Risk of Material Misstatement" flowchart also supports the view that the understanding of controls is factored into the process to identify risks of material misstatement.</p> <p>We believe the first point that needs to be made clear is the identification of a risk of material misstatement versus the assessment of a risk of material misstatement. The next point is in relation to differentiating between having an 'understanding of internal control' (as included in paragraph 4) when identifying risks of material misstatement versus assuming that the entity's controls are operating effectively and thus influencing whether a risk of material misstatement exists or not.</p> <p>Ultimately, the understanding of the internal control structure including the design and implementation of controls is appropriate and required when identifying and assessing risks of material misstatement, however auditors are unable to conclude that there is a remote risk (therefore not a risk of material misstatement) by assuming that one or more controls are operating effectively - this is what needs to be clearly communicated within the standard.</p> <p>Thirdly, it is unclear how inherent risk and control risk interacts and combines together when it comes to assessing the risks of material misstatement.</p>

	<p>For instance, paragraph 5 states <i>"For the identified risks of material misstatement at the assertion level, a separate assessment of inherent risk and control risk is required by this ASA."</i> However no requirements or guidance is provided on how these separate assessments then combine together to form the overall assessment of the risk of material misstatement.</p>
16(h)	<p>Paragraph 16 (h) defines relevant assertions as <i>"An assertion is relevant to a class of transactions, account balance or disclosure when the nature or circumstances of that item are such that there is a reasonable possibility of occurrence of a misstatement with respect to that assertion that is material, individually or in combination with other misstatements. There is such possibility when the likelihood of a material misstatement is more than remote. The determination of whether an assertion is a relevant assertion is made before consideration of controls."</i></p> <p>We recommend that consideration factors or additional guidance be linked or included, in order to assist auditors in determining what constitutes a 'reasonable possibility' or when a possibility would be 'remote'.</p> <p>In addition, this paragraph states that the "determination of whether an assertion is a relevant assertion is made before consideration of controls", which implies that relevant assertions are only applicable to inherent risk and not control risk. This does not envisage scenarios such as when the entity does not have a control over the cut-off assertion, or they do have a control but it is not designed/implemented appropriately. This may potentially lead to an additional relevant assertion (if cut-off was not considered relevant beforehand) that is based on control risk not inherent risk. If this is considered to be part of the inherent risk assessment rather than control risk assessment, then this needs to be made clear so that it sets the scene for the remainder of the standard.</p>
16(k)	<p>The definition of a significant risk is an identified risk of material misstatement for which the inherent risk is close to the upper end of the spectrum of inherent risk. The potential impact of the control risk is not referred to at all.</p> <p>Does this mean that only the inherent risk impacts whether a risk of material misstatement is classified as significant or not? Our view is that the potential for a significant risk may be increased if the entity does not have relevant controls or they were not designed, implemented or operating effectively.</p>
52, A240-A242	<p>Currently the wording of paragraph 52 is as follows:</p> <p><i>"The auditor shall:</i> <i>(a) Identify the classes of transactions, account balances and disclosures that are quantitatively or qualitatively material, and that have not been identified as significant classes of transactions, account balances or disclosures in accordance with paragraph 46; and</i> <i>(b) Evaluate whether the auditor's conclusion that there are no relevant assertions (that is, no related risks of material misstatement) for these classes of transactions, account balances and disclosures remains appropriate."</i></p>

	<p>In addition, this paragraph sits under a sub-heading entitled <i>"Classes of Transactions, Account Balances and Disclosures that are Not Significant, but which are Material"</i>.</p> <p>Linked to our overriding comment above, we highlight that the wording utilised is potentially misleading and confusing due to the reference to 'quantitatively or qualitatively material' and the definition of a significant class of transactions, account balance or disclosure. We question whether it is possible for the auditor to identify a class of transactions, account balance or disclosure that is qualitatively material that has not been identified as significant. Perhaps the reference to a class of transactions, account balance or disclosure that is 'quantitatively material' infers that it is greater than materiality.</p> <p>From our perspective that the purpose of this paragraph is for the auditor to perform a 'sense check' and reassess whether their original conclusions remain true (although this depends on the outcome of our earlier comments relating to significant and material classes of transactions, account balances and disclosures). As a result, we recommend that the wording of paragraph 52(a) be amended to remove reference to 'quantitatively or qualitatively material' so it reads as follows: <i>"The auditor shall:</i> <i>(a) Identify the classes of transactions, account balances and disclosures that have not been identified as significant classes of transactions, account balances or disclosures in accordance with paragraph 46;"</i></p> <p>Paragraph 52 is supported by guidance paragraphs A240-A242. We believe that the content included within paragraphs A241 and A242 does not provide relevant guidance to the auditor and if anything, creates further confusion and ambiguity.</p> <p>Paragraph A241 indicates that there can be transactions, account balances or disclosures that are quantitatively or qualitatively material but are not determined as significant transactions, account balances or disclosures as there are no relevant assertions, and then provides an example that fails to explain or differentiate.</p> <p>Paragraph A242 incorporates a reference to paragraph 18 of ASA 330 which states "irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure". We are struggling to understand how this links to supporting paragraph 52 of ASA 315.</p>
50(a)	<p>Paragraph 50 (a) states that <i>"When the auditor plans to test the operating effectiveness of controls in designing further audit procedures to be performed to respond to a risk of material misstatement at the assertion level, the auditor shall assess control risk at less than maximum."</i></p> <p>The requirement to assess control risk at less than maximum automatically, based on the planned audit strategy does not take into consideration the underlying robustness of the control and whether they will prevent, detect or correct material misstatements, as defined in Paragraph 3.</p> <p>Additionally, the requirement to assess control risk at less than maximum based on the planned audit approach, may not be always be appropriate. Paragraph 53 states:</p>

	<p><i>"the auditor's assessments of the risks of material misstatement at the financial statement level and assertion level <u>may change</u> during the course of the audit as additional audit evidence is obtained."</i></p> <p>which is one example where the control risk may be set at maximum notwithstanding the planned audit approach.</p>
54	<p>We note that this paragraph relating to audit documentation does not have an overarching requirement to indicate that auditors need to use professional judgement in the documentation of the procedures they have performed as part of the risk assessment. The current wording of this paragraph promotes a risk that auditors will interpret paragraph 54 to mean that only the items stipulated require documentation.</p> <p>This paragraph also does not include a requirement to document key considerations and judgements, such as those relating to the stand-back requirement in paragraph 10, nor control deficiencies identified in paragraph 43 or risk assessment procedures performed in paragraph 17.</p> <p>We recommend that an overarching paragraph indicating the requirement to utilise professional judgement be included at the start of this paragraph.</p>
Overriding	<p>As previously mentioned (refer to our response to question 3 in Appendix 1), ED 01/18 should be updated to articulate the expectations and requirements over information prepared by the entity used for risk assessment purposes.</p> <p>Further guidance is needed on what constitutes information produced by the entity that is used for risk assessment purposes, and what the expectations and requirements are in relation to understanding and/or obtaining evidence over the reliability of this information (including the nature, timing and extent of testing).</p>
Clarification and clerical changes to ED 01/18	
5 and 48	<p>These paragraphs make reference to assessing risk based on the magnitude of misstatement, however our view is that the wording should be aligned to the wording in paragraphs A10 and A222 which reference the "potential magnitude" of the misstatement were that misstatement to occur, and "magnitude of the possible misstatement".</p>
6	<p>We noted a repeated comma in the final sentence of this paragraph.</p>



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315
Contact Juliet Low (+61 2 9295 3881)

15 October 2018

Dear Sir

Comment submission on AUASB Exposure Draft ASA 315 Identifying and Assessing the Risks of Material Misstatement

We are pleased to have the opportunity to respond to ASA 315 *Identifying and Assessing the Risks of Material Misstatement* exposure draft (ED) issued by the Australian Auditing and Assurance Standards Board (AUASB). This letter represents the views of KPMG Australia.

We understand that the AUASB intends to respond to the International Auditing and Assurance Standards Board's (IAASB's) invitation to comment on ISA 315 *Identifying and Assessing the Risks of Material Misstatement* ED.

The Global KPMG network is still in the process of developing its response to the ISA 315 ED, which will be submitted in accordance with the IAASB's deadline. Accordingly, our response contained herein is not as extensive as the Global response will be, and should be read in conjunction with the KPMG Global response.

Our overarching comments are set out below. Please refer to Appendix 1 to this letter for our views and responses to the specific questions raised by the AUASB for comment.

Overall, KPMG Australia is supportive of the adoption of the proposed Auditing Standard.

We are supportive of the overall direction of the changes proposed to ASA 315 and believe that these broadly achieve the principal objective of the IAASB in relation to this project, i.e. to establish more robust requirements and appropriately detailed guidance to drive auditors to perform consistent and effective identification and assessment of the risks of material misstatement. We also believe that it reflects the rapidly changing business environment, in particular in relation to the use of information technology, and will better foster independence of mind and the application of professional scepticism.

We believe that the proposals represent considerable enhancements to the extant standard, as they provide a stronger foundation for the auditor's risk assessment process, as well as establishing clearer, more granular, requirements, supported by detailed application guidance as to how and why an auditor needs to adhere to these requirements.

However, we do have concerns about certain aspects of the ED, including its application. Our principal concerns relate to the following:

The navigability of the standard

Although we are supportive of the IAASB's decision that the requirements remain principles-based, we note that as a result they are premised on very lengthy and detailed application material, to a much greater extent than is the case for other ISAs. We believe that this structure compounds the difficulties in understanding the intended flow of the standard, which is already complex as a result of its iterative nature.

The complexity of the standard

We highlight that the level of complexity of the standard may give rise to difficulties and potential scope for inconsistency in application of the standard, in particular for audits of smaller and less complex entities. The application material includes high level considerations regarding scalability of the standard, but we recommend that the IAASB consider the inclusion of further clarification and examples as to scalability.

Uncertainty in application of certain requirements in relation to system of internal control

We believe there is scope for inconsistency in application in relation to how to obtain the required understanding of each component of the system of internal control, which may present challenges for auditors of smaller and less complex entities in particular.

We provide more detailed commentary regarding the above in our responses to question 5, set out in the appendix to this letter.

Requirements relating to identification and assessment of risks of material misstatement

The numerous requirements in paragraphs 45 to 50 seem to unnecessarily complicate the risk assessment process.

Paragraph 45 requires the identification of risks of material misstatements, both at the financial statement and assertion level. Paragraph 46 then goes on to require the determination of significant classes of transactions, account balances and disclosures,

and their relevant assertions, based on these identified risks. Paragraphs 47 to 50 require the assessment of the identified risks of material misstatements at the financial statement and assertion levels. Paragraph 48 requires the assessment of the likelihood and magnitude of material misstatement in the assessment of inherent risk for identified risks of material misstatements at the assertion level. Paragraph 49 then specifically requires the determination of whether any of the assessed risks of material misstatement are significant risks. Paragraph 50 requires the assessment of control risk for identified risks of material misstatements at the assertion level.

In practice, it is likely that the 1) identification of risks of material misstatements, 2) determination of significant classes of transactions, account balances and disclosures, and their relevant assertions, 3) assessment of the likelihood and magnitude of material misstatement in the assessment of inherent risk for identified risks of material misstatements at the assertion level and 4) determination of whether any of the risks of material misstatement are significant risks, will be performed in a single inherent risk assessment step. Instead of requiring these four seemingly discrete steps, we propose that starting point be to assess the likelihood and magnitude of material misstatement at the assertion level, which, if high enough, would give rise to significant classes of transactions, account balances and disclosures, and their relevant assertions, and potentially significant risks. Once this has been performed, control risk and the resultant risk of material misstatement can be assessed.

The first step to separately identify risks of material misstatement in particular appears to be duplicative and creates unnecessary complexity in our view.

Incorporation of data and analytics

Lastly, we suggest that the IAASB further explores the impact of data and analytics (D&A) specifically on risk identification and assessment, in terms of whether and how the nature and/or extent of the risk assessment procedures as currently described may change in an audit environment in which the auditor is able to incorporate all transactions into its risk assessment process. As currently described, D&A techniques would appear to be applied in addition to the current requirements of the standard, rather than being an integral part of a possible approach to risk identification and assessment. Paragraphs A33 and A213 touch on this but at a very high level. We recognise that D&A is an emerging area, and that there is a separate project to consider the implications of this on an audit. However, it would be helpful to further acknowledge this area in the ED.

Should you wish to clarify any aspect of KPMG Australia's submission, I would be pleased to discuss. My contact details are julietlow@kpmg.com.au or (02) 9295 3881.



***Auditing and Assurance Standards Board
Comment submission on AUASB Exposure Draft
ASA 315 Identifying and Assessing the Risks of
Material Misstatement
15 October 2018***

Yours faithfully,

A handwritten signature in blue ink, appearing to read 'Juliet Low'.

Juliet Low
Partner

Appendix 1 – KPMG Australia’s views on specific matters highlighted by the AUASB in the Exposure Draft (ED) ASA 315 Identifying and Assessing the Risks of Material Misstatement

1. Has ED 01/18 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risks of material misstatement. In particular:

(a) Do the proposed changes help with the understandability of the risk identification and assessment process?

(b) Are the flowcharts helpful in understanding the flow of the standard (i.e., how the requirements interact and how they are iterative in nature)? If yes, should they be included in the final ISA 315?

(c) Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6–28 of the IAASB’s Explanatory Memorandum?

(d) Are the new introductory paragraphs helpful?

We are supportive of the overall direction of the changes proposed to ISA 315 and we believe that these are helpful in addressing the public interest issues identified.

In general, we believe that ED 01/18 has provided significant clarification regarding many aspects of the process for the identification and assessment of the risks of material misstatement, in comparison to the extant standard. In particular, the introductory paragraphs, the flowcharts and the increase in “signposts” or “milestones” help with the understandability of the standard, both in terms of the flow, the overall objectives, and how each part of the process supports the achievement of these objectives. In this regard, we recommend that the flowcharts are ultimately included as part of the standard.

Nevertheless, this is a highly complex standard, with much of this complexity residing in the fact that an auditor executes the procedures required in an iterative, rather than a linear fashion, as described in the Explanatory Memorandum to the ED, as well as in the application material. Furthermore, as we describe in our overarching comments, many “steps” are in practice performed concurrently, and in doing so, implicit consideration is given by the auditor to the results or expected results relating to other aspects of the standard. This level of intricacy, which will vary depending on the engagement circumstances, is challenging to describe in the standard itself, and is also very difficult to capture clearly in flowcharts, which therefore summarise the written material but do not provide more meaningful insights as to its application.

We also note in our overarching comments that the requirements are supported by lengthy and detailed application material, to a much greater extent than is the case for other ISAs. We believe that this compounds the difficulties in understanding the intended flow of the standard.

We consider that the standard would particularly benefit from clearer linkage between the “understanding” obtained regarding each of the components of the entity’s system of internal control and how this is applied in fulfilling the requirements to identify and assess the risks of material misstatement at paragraph 45 onwards. Paragraph 17 describes this understanding as forming the basis for the risk identification and assessment. However, the application material, in particular A201 and A202, focuses more on the inter-relatedness of these aspects of the standard, e.g. that the auditor forms initial expectations and then confirms or updates these, or that information gathered in performing the risk assessment procedures to obtain the understanding is used as audit evidence to support the risk assessment. Paragraph A208 states that the identification of risks of material misstatement at the assertion level is performed before consideration of any controls, which seems to contradict this linkage insofar as risks of material misstatement at the assertion level are concerned.

We suggest that the IAASB consider including further enhancements to the ED to avoid confusion and inconsistency in application of the standard, such as, at a minimum, increased cross-referencing between relevant areas of the standard, in particular in respect of steps that may be performed concurrently. We also recommend that the IAASB may wish to explore alternative or additional flowcharts, or a tabular presentation, to provide a more meaningful summary of the simultaneous nature of the performance of certain key requirements, as well as to illustrate where implicit consideration is made of the results of other steps, and where initial expectations are formed, and then refined, during the performance of certain procedures.

We believe that the introductory paragraphs are helpful, as they “set the scene”, help the auditor to navigate this complex standard, and give emphasis to key overarching concepts, including professional scepticism.

2. Are the requirements and application material of ED 01/18 sufficiently scalable, including the ability to apply ED 01/18 to the audits of entities with a wide range of sizes, complexities and circumstances?

We are supportive of the overall approach taken by the IAASB regarding scalability of the ED, i.e. the establishment of principles-based requirements, supported by detailed application material, including guidance and examples as to how to apply the requirements across entities that vary significantly in terms of size and complexity.

We note that the Explanatory Memorandum, at paragraph 36, states that *“clarifying the requirements related to the understanding of each component of the system of internal control is an important aspect of the proposed enhancements to the standard. Within each component, the IAASB has set out the matters that need to be understood, as well as providing further guidance about the extent and scalability of related procedures, as appropriate.”*

In connection with the above, we welcome, in particular the following enhancements:

- recognition that aspects of the system of internal control may be less detailed / formalised in smaller and less complex entities;
- clarification regarding understanding of the IT environment / identification of risks arising from IT and identification and evaluation of GITCs relevant at smaller and less complex entities;
- recognition that complexity as well as, or even more so than, size of an entity is important. We also support the description of smaller and less complex entities being at one extreme, to help provide a reference point as to how the auditor would apply judgement (paragraph A224) and take into account the nature and circumstances of each entity.

It would be helpful if the IAASB could provide examples as to the execution of certain requirements. The application material contains theoretical guidance that the nature and extent of procedures may vary according to the audit circumstances, including the size and complexity of the entity subject to audit, but this material would benefit from more detailed examples.

Furthermore, the documentation requirements, in their specificity, may be onerous for audits of smaller and less complex entities, as implicitly the judgements in identifying and assessing risks of material misstatement may be difficult to specifically describe. We suggest that the IAASB provide further guidance as to what would be expected in terms of documentation in this area, in particular, the extent to which judgements made en route to a final determination need to be included. We believe it is also critical to clarify the extent of documentation required where, for example, a risk is not significant. While paragraph A245 acknowledges that the auditor is not required to document “every inherent risk factor that was taken into account”, more clarity on the expected extent of documentation will be critical in our view for consistency of application.

3. Do respondents agree with the approach taken to enhancing ED 01/18 in relation to automated tools and techniques, including data analytics, through the use of examples to illustrate how these are used in an audit (see Appendix 1 of the IAASB’s Explanatory Memorandum for references to the relevant paragraphs in ED 01/18)? Are there other areas within ED 01/18 where further guidance is

needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?

We agree with the approach taken and find the illustrative examples helpful. We believe that this is appropriate in terms of the objective of modernizing the standard and making it fit for purpose in today's technological environment.

We are supportive of the approach to avoid the use of terminology that is overly precise/ narrow, or that may be understood differently by various groups, as this is a rapidly emerging field and we recognise the IAASB's intention not to outdate itself at the outset.

However, we suggest that the IAASB further explores the impact of Data and Analytics (D&A) specifically on risk assessment, in terms of whether and how the nature and/or extent of the risk assessment procedures as currently described may change in an audit environment in which the auditor is able to incorporate all transactions into its risk assessment process. As currently described, D&A techniques would appear to be applied in addition to the current requirements of the standard, rather than being an integral part of a possible approach to risk identification and assessment. Paragraphs A33 and A213 touch on this but at a very high level. We recognise that this is an emerging area, and that there is a separate working group/ project to consider the implications of D&A on an audit. However, it would be helpful to further acknowledge this area in the ED.

4. Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk identification and assessment process? Do you support the proposed change for the auditor to obtain 'sufficient appropriate audit evidence' through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional scepticism?

Overall, we believe that the proposals are helpful in supporting the appropriate exercise of professional scepticism throughout the risk identification and assessment process. In particular, we agree with the principles-based approach and reference to the concept of professional scepticism in an overarching fashion in the introductory paragraphs, rather than the inclusion of several, individually prescriptive requirements, throughout the standard. We believe that this approach is aligned to the current description of professional scepticism being a mindset/ fundamental behaviour of an auditor.

With regard to the proposal to include a requirement in paragraph 17 for the auditor to "obtain sufficient appropriate audit evidence as a basis for the identification and assessment of risks of material misstatement", we do not consider this concept to be

applicable to separate “steps” in this auditing standard. This terminology is understood in a broader context and the proposed approach does not recognise the cohesive nature of an audit as a whole.

Accordingly, we suggest that the IAASB considers revising the requirement to remove the reference to “sufficient, appropriate” when describing audit evidence.

5. Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks or material misstatement? Specifically:

(a) Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?

(b) Have the requirements related to the auditor’s identification of controls relevant to the audit been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?

(c) Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor’s understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor’s consideration of the effects of the entity’s use of IT on the identification and assessment of the risks of material misstatement?

We are supportive of the IAASB’s aims in enhancing and clarifying this area, as we consider that much of the complexity and scope for inconsistency of application in practice lies in obtaining this understanding. In particular, we welcome the alignment of the categorisation of the components of the system of internal control to the COSO Framework, and therefore the order in which the components of internal control are presented. Additionally, the requirements include greater focus on why we obtain the understanding, with a number of “signposts” or “milestones” that require the auditor to make an evaluation.

However, we suggest that the IAASB consider clarifying that any ‘evaluation’ is made in respect of the overarching objectives of the standard as a whole, and not in respect of any specific matter in isolation.

We believe there is scope for inconsistency in application in relation to how to obtain the required understanding of each component of the system of internal control, which may present challenges for auditors of smaller and less complex entities in particular.

For example, we believe there is an intentional difference in respect of the understanding obtained over the information system and communication component of the system of internal control, and that an auditor is required to identify the controls relevant to financial reporting that are embedded in this component and to evaluate the design of this system by evaluating the design and implementation of these controls, but is not required to perform a similar evaluation in respect of the controls in the other components, other than to identify whether there are any controls relevant to the audit within these components. We suggest that the IAASB clarify whether this is an intentional difference.

We believe that the ED may give rise to uncertainty and inconsistency in application with regards to the understanding that is required to be obtained in respect of the information system and communication component of the system of internal control at paragraph 35(a)–(d) and how this relates to the evaluation of the design and implementation of the information system controls relevant to financial reporting required by paragraph 36. It is unclear whether the requirement at paragraph 36 is achieved through the performance of paragraph 35, or whether it is considered as part of the performance of paragraph 35. This is compounded by a lack of clarity as to how this understanding is obtained.

Furthermore, we are concerned that the ED does not sufficiently clarify which controls reside in the information systems component and which in the control activities component and how these interrelate, if at all.

At paragraph 37 of the EM, the IAASB notes that “Controls relevant to the audit are primarily direct controls and controls in the controls activities component. However, the auditor may identify certain controls in the control environment, the entity’s risk assessment process or the entity’s process to monitor controls as relevant to the audit because they address risks of material misstatement at the assertion level.”

The above leads to a lack of clarity as to the distinction between the nature of the controls in the information system component and the control activities component, including whether controls over the flow of information are direct and why controls in the information system component are relevant to financial reporting whereas controls in the control activities components are relevant to the audit, and how these concepts are connected. There is also uncertainty in relation to the work needing to be performed over controls that are relevant to financial reporting.

We consider that the standard would particularly benefit from clearer linkage between the “understanding” obtained regarding each of the components of the entity’s system of internal control and how this is applied in fulfilling the requirements to identify and assess the risks of material misstatement at paragraph 45 onwards. Paragraph 17

describes this understanding as forming the basis for the risk identification and assessment. However, the application material, in particular A201 and A202, focuses more on the inter-relatedness of these aspects of the standard, e.g. that the auditor forms initial expectations and then confirms or updates these, or that information gathered in performing the risk assessment procedures to obtain the understanding is used as audit evidence to support the risk assessment. Paragraph A208 states that the identification of risks of material misstatement at the assertion level is performed before consideration of any controls, which seems to contradict this linkage insofar as risks of material misstatement at the assertion level are concerned. The reference to “significant classes of transactions, account balances and disclosures” in the requirement at paragraph 35(a), in relation to the understanding of the information system relevant to financial reporting, also seems to contradict the notion that the understanding of this component of internal control is considered in identifying the risks of material misstatement, i.e. significant classes of transactions, account balances and disclosures).

We welcome the additional granularity regarding the types of controls that are relevant to the audit in paragraph 39. We also find the clarification in the application material that most controls, although not necessarily all, that are relevant to the audit will be direct controls, and that these will reside in the Information System and Communication, and Control Activities components, helpful.

Notwithstanding the above, this is a complex area. We recommend that the IAASB introduce further clarity regarding paragraph 39(e), which refers to controls for which it is appropriate to evaluate their design and determine whether they have been implemented to enable the auditor to identify and assess the risks of material misstatement at the assertion level. This is difficult to implement – how can you “know what you don’t know” unless you identify and evaluate all the controls. We believe that this concern applies irrespective of the size or nature of the entity, although the work effort to identify these controls may seem disproportionate in a smaller entity.

We support the introduction of the new IT-related concepts and definitions and agree that these are necessary to ensure that ASA 315 remains fit for purpose in a modern environment.

In respect of the IT environment, we note that the description/ definition at A7 and A8 is very technical and may not be clearly understood by auditors.

6. Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:

- (a) Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments’?**
- (b) Do you support the introduction of the concepts and definitions of ‘inherent risk factors’ to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor’s risk assessment process?**
- (c) In your view, will the introduction of the ‘spectrum of inherent risk’ (and the related concepts of assessing the likelihood of occurrence, and magnitude, of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?**
- (d) Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e., an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion), and how they assist the auditor in identifying where risks of material misstatement exist?**
- (e) Do you support the revised definition and related material, on the determination of ‘significant risks’? What are your views on the matters presented in paragraph 57 of the IAASB’s Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?**

We support the separate assessments of inherent and control risk at the assertion level, and we consider that the related requirements and guidance are clear. We believe this amendment results in better alignment to ASA 330.7, which requires the auditor to consider inherent risk and control risk separately in order to respond, and it also aligns to the amendments already made to ISA 540 in this regard.

As discussed above, we suggest that the IAASB consider whether the concept of ‘identification of a risk of material misstatement’ (versus assessment of a risk of material misstatement) can be dropped, given the separation of assessments of inherent and control risk.

We are supportive of the introduction of the “spectrum of inherent risk” and believe that this will help us to understand that this may vary smoothly, rather than being the binary assessment of significant versus non-significant that we make at present. We are also supportive of the IAASB’s conclusion to retain the concept of significant risk on the basis that other ISAs contain the concept of significant risk and therefore ISA 315 needs to align to this.

Together with the updated definition of significant risk, the concept of a spectrum of inherent risk helps the auditor to focus on the nature of the risks themselves, rather than requiring a determination as to whether a risk is significant based on the expected audit response, i.e. whether the risk requires “special audit consideration”.

We support the IAASB’s preliminary conclusion that significant risks are best represented by a high likelihood of occurrence or high magnitude of potential misstatement (rather than ‘and’), and consider that the auditor will apply its professional judgement as to whether a matter is actually a significant risk.

However, we have some concerns about the description in A229 that significant risks are “assessed close to the upper end of the spectrum” and suggest referring instead to “at the upper end of the spectrum”.

We are supportive of the inclusion of the new concepts and related definitions, however, we recommend that the IAASB provides further information to support the definitions, such as examples of “classes of transactions” and “account balances” and the distinction between the two.

We note that one of the intentions of the IAASB is to clarify the scope of the auditor’s understanding of the information system, and the auditor is required at ED 01/18.35(a) to “understand how information relating to significant classes of transactions, account balances and disclosures flows through the entity’s information system.” We believe that this is helpful as it clarifies when such understanding needs to be obtained.

We also support revisions to the definition that better focus on a significant risk being assessed by reference to the spectrum of inherent risk, rather than on the response to the risk. It better enables compliance with the requirement in the extant standard at paragraph 27 to identify significant risks excluding the effects of controls, i.e. based on the inherent risk alone.

7. Do you support the additional guidance in relation to the auditor’s assessment of risks of material misstatement at the financial statement level, including the determination about how, and the degree to which, such risks may affect the assessment of risks at the assertion level?

Yes, the guidance better clarifies how risks that affect a number of assertions have a more pervasive effect on the financial statements and therefore need to be assessed to develop overall responses, as well as the consideration of how such risks affect the assessment of risks of material misstatement at the assertion level.

8. What are your views about the proposed stand-back requirement in paragraph 52 of ED 01/18 and the proposed revisions made to paragraph 18 of ASA 330 and its supporting application material? Should either or both requirements be retained? Why or why not?

We do not believe that it is critical that ED 01/18 include a standback requirement, since there is greater emphasis now on the iterative nature of the risk assessment process, as well as the increased clarity in respect of how and why to perform each step.

However, given the complexity of the standard and the fact that many of the steps are performed concurrently, which necessitates the auditor to continually update its understanding and consideration of views formed and assessments made, we believe that overall it may be helpful to have a standback at the end of the risk assessment process, before the auditor proceeds to the execution of responses.

We do not consider it appropriate to retain the standback at ISA 330.18, as we believe that the placement of this requirement at a relatively advanced stage of the audit, as well as the specific language used ("irrespective of [the risk identification and assessment procedures performed]") may serve to reduce the emphasis on the risk identification and assessment process as a critical part of the audit process.

9. Other requests for comment

We do not have any other specific comments in respect of the questions posed.

We believe the effective date to be a reasonable implementation period.

Australian specific questions

10. Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

We believe the applicable laws and regulations have been appropriately addressed and no references to relevant laws or regulations have been omitted.

11. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

We do not believe any applicable laws and regulations may impact or conflict with the proposed standard.

12. Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

We are not aware of any principles and practices that may impact the application of or conflict with the proposed standard.

13. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the

requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

- (a) Where those costs are likely to occur;**
- (b) The estimated extent of costs, in percentage terms (relative to audit fee); and**
- (c) Whether expected costs outweigh the benefits to the users of audit services?**

We expect to incur costs associated with training and coaching auditors to apply the changes in requirements. It is difficult to estimate the extent of costs or the proportion of audit fee, as each audit will be impacted in a different manner depending on its size and complexity. We consider that the increase in costs will generally benefit audit quality and therefore the users of audit services.

However, we note that incremental costs may be incurred where the auditor is required to comply with the documentation requirement in paragraph 54(d) relating to the rationale for the significant judgements made in identifying and assessing the risks of material misstatement. We expect that the more extensive documentation requirement in paragraph 54(d) of the ED will increase the time spent on documentation, particularly for smaller firms, without an associated benefit for users of audit services.

14. What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 315 (specific questions/examples would be helpful).

Considering the current status of the ISA 315 project, we cannot at this time identify specific implementation guidance that we would like the AUASB to issue in conjunction with the release of ASA 315.

15. Are there any other significant public interest matters that stakeholders wish to raise?

No, there are no other significant public interest matters that we wish to raise.

ED 315 ROUNDTABLES

SUMMARY OF FEEDBACK

Question 1: Has ED 01/18 been appropriately restructured, clarified and modernised in order to promote a more consistent and robust process for the identification and assessment of the risks of material misstatement. In particular:	Roundtable	ATG Comments
<p>a) Do the proposed changes help with the understandability of the risk identification and assessment process?</p> <ul style="list-style-type: none"> Overall good improvement on extant 315, but long and complex, particularly with so many terms and inter-relationships. Will this make the process more robust? Yes probably. Definition of significant class of transactions, account balances, disclosures, relevant assertion, significant risk – confusing. Concerned won't be consistently applied due to the complexity and the judgements required. 	All	Include in submission
<p>b) Are the flowcharts, prepared by the IAASB, helpful in understanding the flow of the standard (i.e., how the requirements interact and how they are iterative in nature)? If yes, should they be included in the final Standard?</p> <ul style="list-style-type: none"> Different views on flow of the standard. <ul style="list-style-type: none"> Positive <ul style="list-style-type: none"> Whilst the standard was 'circular' the flow made sense. Iterative process. Initial identification of ROMMs before SCOTABDs¹ forces you to look more widely at risks, before getting into detail. That's good. Throughout process continually identifying and assessing ROMMs. BUT need flowcharts to help understand so shows it is complex. Alternative view <ul style="list-style-type: none"> In practice identify SCOTABDs before ROMM but ED has identify ROMMs before you've identified SCOTABDs? Identification of SCOTABDs too late in the process paragraph 35 refers to SCOTABDs before you've identified them yet? Overwhelming support for the flowcharts as an appendix to the standard 	<p>Perth – mixed but a stronger view that it was in the wrong order</p> <p>All</p>	Majority view was that the order and flow was ok. But iterative process made it complex.
<p>c) Will the revisions promote a more robust process for the identification and assessment of the risks of material misstatement and do they appropriately address the public interest issues outlined in paragraphs 6–28 of the IAASB's Explanatory Memorandum.</p>		

¹ Significant class of transactions, account balances, disclosures

No issues raised		
<p>d) Are the new introductory paragraphs helpful?</p> <ul style="list-style-type: none"> Mainly positive feedback <ul style="list-style-type: none"> Overall helpful but shows how complex the standard is. Should be incorporated within the requirements and introduced where terms are actually used <ul style="list-style-type: none"> For example: spectrum of inherent risk not in requirements, Separation of IR and CR is clear in introductory, but less clear in requirements. But alternate view: <ul style="list-style-type: none"> Para 4 needs to be clearer, too wordy and needs to be read numerous times. Inconsistent with para 7. para 4 identification of ROMMs is before controls, assessment of ROMMs is after controls? Does this make sense? 	<p>Most</p> <p>Perth</p>	<p>Majority view that introductory paragraphs are helpful but more should be in requirements. To be included in draft submission.</p> <p>Only noted in Perth. Submission to include complexity of para4</p>
<p>Question 2 – Are the requirements and application material of ED 01/18 sufficiently scalable, including the ability to apply ED 01/18 to the audits of entities with a wide range of sizes, complexities and circumstances?</p> <ul style="list-style-type: none"> Concept of small and less complex supported. But majority prefer just complex ie. size not relevant Complexity will be harder for SMPs. Consider guidance for mainly substantive approaches Definition of relevant assertion ie. “less than remote” makes scalability a real challenge. ie. hard to justify an assertion not being relevant, and COTABD not being significant Paragraph 39 will create problems for scalability as will require more controls work. Don’t agree with having to test D & I of journals for very small audit ITGCs adds another layer of complexity. Does this mean ITGCs on every engagement – almost every engagement would be dependent on IT applications other than micro type engagements (eg SMSF) Inherent risk factors help focus attention and while there is more to digest, the upfront rationale may aid in a more efficient audit approach Documentation demonstrates scalability by the use of the word KEY – the level of granularity in the documentation requirement is seen as a positive. Would like better guidance on the extent of documentation required. 	<p>Feedback was consistent in all roundtables</p>	<p>To be included in draft submission</p>
<p>Question 3 - Do stakeholders agree with the approach taken to enhancing ED 01/18 in relation to automated tools and techniques, including data analytics, through the use of examples to illustrate how these are used in an audit (see Appendix 1 of the IAASB’s Explanatory Memorandum for references to the relevant paragraphs in ED 01/18)? Are there other areas within ED 01/18 where further guidance is needed in relation to automated tools and techniques, and what is the nature of the necessary guidance?</p>		

<ul style="list-style-type: none"> • Overall support the references to automated tools and techniques in the application material. • Not enough– was expecting the standard to go further • Concern there should be more guidance / examples about how you can use Data Analytics / Technology as a means to identify and assess risks. • Concern that standard should have mechanisms where use of Data / Technology techniques can be used as a substitute for requirements in ISA 315. • How far do you need to test data used at the risk assessment stage? Do you need to test ITGC before you use data sets used in risk assessment? 	All	
<p>Question 4 - Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk identification and assessment process? Do you support the proposed change for the auditor to obtain ‘sufficient appropriate audit evidence’² through the performance of risk assessment procedures to provide the basis for the identification and assessment of the risks of material misstatement, and do you believe this clarification will further encourage professional scepticism?</p> <ul style="list-style-type: none"> • General view is that whilst the standard has more robust requirements and will result in more work – this doesn’t necessarily mean more professional sceptical. Professional scepticism is an attitude, a standard cant enforce. • General disapproval of the use of the term “sufficient appropriate audit evidence” in paragraph 17. Extant 315 uses the term “form the basis”. • Need a different term which is a halfway house increasing evidentiary requirements for risk assessment but acknowledging it doesn’t need to be at the same level as required under ISA 500. • Concern about the interaction of the increased professional scepticism requirements and more granular risk assessment process diminishing the work done in this area, specifically in relation to Fraud risk assessment. • Shouldn’t paragraph 54 reference paragraph 17? Paragraph 54 needs to have enough to achieve paragraph 17. 	<p>Consistent view</p> <p>Melbourne, Perth, Canberra</p> <p>Brisbane</p>	Include in submission.
<p>Question 5 Do the proposals made relating to the auditor’s understanding of the entity’s system of internal control³ assist with understanding the nature and extent of the work effort required and the relationship of the work effort to the identification and assessment of the risks or material misstatement? Specifically:</p> <p>a) Have the requirements related to the auditor’s understanding of each component of the entity’s system of internal control been appropriately enhanced and clarified? Is it clear why the understanding is obtained and how this informs the risk identification and assessment process?</p>	All	

² See paragraph 27 of the IAASB’s Explanatory Memorandum and paragraph 17 of ED 01/18
³ Paragraphs 25-44 and A89-A200 of ED 01/18

<ul style="list-style-type: none"> • More granular requirements are good. • Concern in relation to understanding control environment particularly 27(a) and 27(d) – whilst these aspects are important, how do you demonstrate you have met these requirements? Suggestion is to write these requirements from the negative ie. have you identified any evidence not in place... Consider that more examples are required. • Paragraph 29 should be just for FS risks • Spell out what component 4 really means and clarify how component 4 and 5 interact. • Should include a reference to IIA Standards in the Internal Audit content ie. when assessing competency etc. • Size is redundant eg A166, A167, consider removing. 	<p>All</p> <p>Perth</p> <p>Melbourne</p> <p>Sydney</p> <p>Canberra /Hobart</p>	
<p>b) Have the requirements related to the auditor’s identification of controls relevant to the audit⁴ been appropriately enhanced and clarified? Is it clear how controls relevant to the audit are identified, particularly for audits of smaller and less complex entities?</p> <ul style="list-style-type: none"> • More integration of the IT environment within the Internal Controls paragraphs required. • Paragraphs 39 – 42 clear and what should be happening <ul style="list-style-type: none"> ○ Possible increase in number of controls which are relevant to the audit, more assertions are in play due to “more than remote” which means there are more controls. ○ What is the intention of para. 39 (c) – if it is for fraud, then ASA 240 sufficiently covers this, if it is for another reason it is not clear (roundtable struggled to think of anything other than fraud, perhaps other errors). ○ What is the intention of para. 39 (e) – not clear why this sub-paragraph has been added. ○ Concern around application for less complex entities. Doing D&I not always appropriate for smaller audits ○ D & I over journals shouldn’t be for every audit particularly where fully substantive ○ What are the implications of wanting to take a fully substantive approach? 	<p>Canberra</p> <p>All</p> <p>Melbourne / Sydney</p> <p>All</p> <p>Brisbane</p> <p>Brisbane</p> <p>All</p>	
<p>c) Do you support the introduction of the new IT-related concepts and definitions? Are the enhanced requirements and application material related to the auditor’s understanding of the IT environment, the identification of the risks arising from IT and the identification of general IT controls sufficient to support the auditor’s consideration of the effects of the entity’s use of IT on</p>		

⁴ See ED 01/18, paragraphs 39-40 and paragraphs 37-40 of the IAASB’s Explanatory Memorandum

<p>the identification and assessment of the risks of material misstatement?</p> <ul style="list-style-type: none"> • All the IT aspects are seen as a positive • Para. 35 (understanding of IT controls) and para. 36 (design and implementation) are two separate steps in the standard, logically should be done as one. • Confusion as to when general controls are tested – on all engagements? Concern scalability. • Not enough risk factors with new technologies • Definition of 16a – is this appropriate? Not framed as an IT application controls, but the term is IT centric • Relevant to the audit – this is clear but concern this will increase the number of controls. More assertions in play, means more controls in play. 	<p>All Melbourne</p> <p>Perth, Brisbane</p> <p>Canberra</p> <p>Canberra</p> <p>All</p>	
<p>Question 6 - Will the proposed enhanced framework for the identification and assessment of the risks of material misstatement result in a more robust risk assessment? Specifically:</p> <p>(a) Do you support separate assessments of inherent and control risk at the assertion level, and are the revised requirements and guidance appropriate to support the separate assessments’?⁵</p> <ul style="list-style-type: none"> • Support for separate assessment. • Research shows hard to do in practice. Do we subconsciously consider controls when assessing? • How you combine IR and CR to get to ROMM is unclear. <p>(b) Do you support the introduction of the concepts and definitions of ‘inherent risk factors’ to help identify risks of material misstatement and assess inherent risk? Is there sufficient guidance to explain how these risk factors are used in the auditor’s risk assessment process?</p> <ul style="list-style-type: none"> • Support for the inherent risk factors • Do you need to document each IRF for all assertions? (no per application material) • Should size be an inherent risk factor? <p>(c) In your view, will the introduction of the ‘spectrum of inherent risk’ (and the related concepts of assessing the likelihood of occurrence, and magnitude, of a possible misstatement) assist in achieving greater consistency in the identification and assessment of the risks of material misstatement, including significant risks?</p> <ul style="list-style-type: none"> • Mainly support for the concept but needs more explanation. • Not sure it will result in consistency as upper end is judgemental. Does this need to be defined? • Too abstract, too hard to evidence and support. • What documentation is expected re likelihood and magnitude and assessment of where you are at on the spectrum 	<p>All</p>	<p>Consistent feedback in submission</p>

⁵ Paragraphs 45-50 and A201-A235 of ED 01/18.

<p>(d) Do you support the introduction of the new concepts and related definitions of significant classes of transactions, account balances and disclosures, and their relevant assertions? Is there sufficient guidance to explain how they are determined (i.e., an assertion is relevant when there is a reasonable possibility of occurrence of a misstatement that is material with respect to that assertion),⁶ and how they assist the auditor in identifying where risks of material misstatement exist?</p> <ul style="list-style-type: none"> • Total consensus that the definition of relevant assertion is not right. More than remote isn't the same as reasonable possibility. Needs to explicitly state that they are the same. • Research supports they are different. • Will result in inconsistent application, and more relevant assertions, significant accounts etc. <p>(e) Do you support the revised definition,⁷ and related material, on the determination of 'significant risks'? What are your views on the matters presented in paragraph 57 of the IAASB's Explanatory Memorandum relating to how significant risks are determined on the spectrum of inherent risk?</p> <ul style="list-style-type: none"> • Concern re what might be defined as what is at the 'Upper End'; • Majority think should be likelihood and magnitude, rather than 'or'. Or a combination. • But support for the idea that the definition should have more of a detailed definition describing how a combination of magnitude and likelihood may be appropriate. • Why is it OR in the SR definition, but AND in para 47 when assessing IR at the assertion level? • Expect that more significant risks will be identified • Does not tie well to management risk assessment process (if entity has the process in place and has identified "significant risks" is there a specific tie back to what the entity has identified). Area could be beefed up. • 		
<p>Question 7 Do you support the additional guidance in relation to the auditor's assessment of risks of material misstatement at the financial statement level,⁸ including the determination about how, and the degree to which, such risks may affect the assessment of risks at the assertion level?</p> <ul style="list-style-type: none"> • Generally supportive • Concern re circular references re process of measurement of financial statement level risk in para 47. • Alternate view – para 47 fine – what happens in practice. practically this may be of concern as people tend to shy away from documenting financial statements risks as don't know how to address 	All	
<p>Question 8 What are your views about the proposed stand-back requirement in paragraph 52 of ED 01/18 and the proposed revisions made to paragraph 18 of ASA 330 and its supporting</p>		

⁶ See footnote 26 of the IAASB's Explanatory Memorandum.
⁷ Paragraphs 16(k) and A10, and A229-A231 of ED 01/18.
⁸ Paragraphs 47 and A215–A220 of ED 01/18.

<p>application material? Should either or both requirements be retained? Why or why not?</p> <ul style="list-style-type: none"> • No major concern with the standback provision as a concept, but <ul style="list-style-type: none"> ○ concern with how the auditor demonstrates and documents this - will create a 'checklist approach' ○ concern will raise expectation of documentation around why each assertion isn't relevant. ○ Misalignment with 330 – If you don't assess a risk in 315, stand-back in 330 tells you if it is material you need to do something, which, properly going through 315 you wouldn't have assessed a risk. 330 stand-back then needs you to pick an assertion and do something when your 315 procedures said no risk for any assertions. • Alternate view - Don't need it as ASA 315 robust process and ASA 330 sufficient • On balance – remove in 330 	<p>All</p> <p>Perth , Canberra</p> <p>Melbourne</p> <p>Melbourne</p> <p>All</p>	
<p>Other matters raised:</p> <ul style="list-style-type: none"> • There's not enough consideration of service provider entities in the public sector where you may audit both organisations – additional guidance is required. • Could have something like appendix 4 (ITGCs) covering cyber security considerations • Concern that public sector examples are not really specific to the public sector. Need to be more specific. • No compelling reasons identified 		



AUASB Board Meeting Summary Paper

AGENDA ITEM NO. 3.1.1

Meeting Date: 29 October 2018

Subject: ED ASA 540 *Auditing Accounting Estimates and Related Disclosures*

Date Prepared: 16 October 2018

☒ Action Required

☐ For Information Purposes Only

Agenda Item Objectives

1. To consider responses and disposition of responses received on Exposure Draft 03/18 Proposed Auditing Standard ASA 540 *Auditing Accounting Estimates and Related Disclosures* (ED 03/18) and Exposure Draft 04/18 Proposed Auditing Standard 2018-2 *Amendments to Australian Auditing Standards* (ED 04/18); and
2. To provide feedback/input and agree on any compelling reasons that need to be considered in the final ASA 540.

Background

1. Exposure drafts ED 03/18 and ED 04/18 were issued on 7 August 2018 for a 70 day exposure period that ended 15 October 2018. The ED comprised an explanatory memorandum supporting a revised ASA 540 and an amending standard dealing with conforming amendments.
2. The AUASB received submissions / comments from 12 stakeholders.

Considerations

Submissions Received

- The AUASB technical group (ATG) received 7 formal submissions in relation to ED ASA 540. One submission put forward a potential compelling reason to amend the standard. The disposition of all comments received is included as Agenda Item 3.2.0.
- Three firms* confirmed via email that they would not be providing a submission on ED ASA 540, on the basis that their global firms responded to the international exposure draft. No compelling reasons to amend the standard were identified.
- The ATG received two# emails supportive of the AUASB approving ASA 540 for release. No compelling reasons to amend the standard were identified.

* Grant Thornton, Deloitte, BDO
CAANZ and HLB Mann Judd

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Feedback from Roundtables

The ATG held roundtables in Perth, Hobart, Canberra, Brisbane, Sydney and Melbourne in September and October 2018 where ED ASA 540 was discussed and questions on exposure considered by stakeholders.

The ATG sought feedback specifically on compelling reasons to amend the standard as well as specific comments on the paragraphs highlighted in the Explanatory Memorandum.

Stakeholder feedback was consistent in supporting the adoption of ED ASA 540 without modification.

Other National Standard Setters

NZAuASB

The NZAuASB at their 24 October 2018 meeting approved the final ISA (NZ) 540 (Revised) and related Conforming Amendments to ISAs (NZ) with no NZAuASB compelling reasons identified.

Canada and UK

The Canadian and UK standard setter intend to approve and issue the final ISA 540 with no proposed amendments to the ISA.

“Compelling Reasons” Assessment

The AUASB is requested to specifically consider the disposition of comments paper (Agenda Item 3.2.0), Exhibit 1, Question (b).

Based on the ATG’s assessment of submissions received, feedback from the roundtables and consideration of other national standard setters, the AUASB technical group have not identified any compelling reasons, in accordance with the [Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board \(IAASB\) and Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board \(NZAuASB\) \(August 2014\)](#), to be made to modify IAASB standards. This document is included as Agenda Item 3.3.

AUASB Technical Group Recommendations

The ATG recommend that the final ASAs are prepared for approval at the 4 December 2018 AUASB meeting, on the basis of the equivalent ISAs with no compelling reason amendments to the ISA.

Next Steps

1. The ATG will bring final ASA 540 *Auditing Accounting Estimates and Related Disclosures* and final ASA 2018-2 *Amendments to Australian Auditing Standards* to the 4 December 2018 meeting for the AUASB to vote for issuance of the standards, with a view to releasing these standards in late 2018; and
2. Based on the AUASBs approval of ASA 2018-2, the ATG will prepare the impacted compiled standards to be approved for release by the Chair and Technical Director in early 2019.

Material Presented

Agenda Item 3.1.1	AUASB Board Meeting Summary Paper
Agenda Item 3.2	AUASB Comments Received and Proposed Disposition Paper
Agenda Item 3.2.1	Comment letter from R1 (confidential submission)
Agenda Item 3.2.2	Comment letter from IPA
Agenda Item 3.2.3	Comment letter from ACAG
Agenda Item 3.2.4	Comment letter from CPA
Agenda Item 3.2.5	Comment letter from KPMG
Agenda Item 3.2.6	Comment letter from PWC
Agenda Item 3.2.7	Comment letter from EY
Agenda Item 3.3	<u>Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board (IAASB) and Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board (NZAuASB) (August 2014)</u>



AUASB Comments Received and Proposed Disposition Paper

AGENDA ITEM NO. **3.2.0**

Meeting Date: 29 October 2018

Subject: Auditing Accounting Estimates and Related Disclosures

Date Prepared: 16 October 2018

Document Type: Exposure Draft

Document Number: ED 03/18 and ED 04/18

Proposed Type & No: Auditing Standard ASA 540

Proposed Title: *Auditing Accounting Estimates and Related Disclosures*

	Page Number
EXHIBIT 1: Responses to Specific Questions	2
EXHIBIT 2: Other General Comments	19

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LISTING OF RESPONDENTS

Short Form Name	Name	Agenda Item Reference
R1	Respondent 1 (confidential submission)	3.2.1
IPA	Institute of Public Accountants	3.2.2
ACAG	Australian Council of Auditors General	3.2.3
CPA	CPA (Australia)	3.2.4
KPMG	KPMG	3.2.5
PwC	PwC	3.2.6
EY	Ernst & Young	3.2.7

EXHIBIT 1 – RESPONSES TO SPECIFIC QUESTIONS

- (a) **Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?**

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	None Noted	-	N
IPA	None Noted	-	N
ACAG	None Noted	-	N
CPA	None Noted	-	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
KPMG	None noted	-	N
PwC	None noted	-	N
EY	None noted	-	N

(b) Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	None Noted	-	N
IPA	None Noted	-	N
ACAG	None Noted	-	N
CPA	None Noted	-	N
KPMG	A blurring of the lines between the auditor's and management's responsibilities could occur where the auditor is required by paragraph 27(b) to develop a point estimate or range. This may conflict with legal requirements for the auditor to be independent in fact and appearance. Paragraph A116 refers to this possibility. However, the standard currently leads to a modified opinion if the auditor cannot develop a point estimate or range without compromising independence. A more proportionate outcome could be obtained if paragraph 27(b) was amended.	Testing how management made the estimate (paragraph 18(b)), is one of these testing options. Under this testing option, and where in the auditor's judgement, management has not taken appropriate steps to understand or address estimation uncertainly, the auditor is directed to paragraph 27. In the IAASB's Basis of Conclusions, the IAASB recognised that to further address concerns raised on ED about the auditor assuming the responsibilities of	N

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Respondent Comment	Commentary	Change to be made to Doc? Y/N
<p>As set out below, we have significant concerns with paragraph 27(b), which prescribes one specific response to circumstances outside the auditor's control, over and above additional procedures required by paragraph 27(a).</p> <p><i>In relation to sub paragraph 27(a):</i></p> <p>While subparagraph 27 (a) emphasises the importance of management's responsibility to perform the necessary procedures to understand and address estimation uncertainty, we have the following concerns:</p> <ul style="list-style-type: none"> • We have reservations about the effectiveness of this requirement because management, as the preparers of financial statements including estimates, are not obliged to comply with auditing standards but with accounting standards. The requirement for management to understand and address estimation uncertainty does not currently reside within the accounting standards. Thus, the requirement on the auditor to request "management to perform additional procedures to understand estimation uncertainty or to address it" is not backed by a similar obligation on the preparer. We recommend the AUASB engage in discussions with the AASB to insert a similar requirement to the same effect within the accounting standards. • Without an equivalent requirement on management, paragraph 27(a) is essentially redundant and requires an additional work effort from the auditor which could be avoided by defaulting to paragraph 27(b). 	<p>management, a requirement was added for the auditor to first request management to perform additional procedures (para 27(a)), additionally the IAASB added the application paragraphs in relation to assessment of independence. In the overall evaluation and based on audit procedures performed, where the auditor is unable to obtain sufficient appropriate audit evidence, the auditor evaluates the implications on the audit or the auditor's opinion.</p> <p><i>Concerns in relation to paragraph 27(a):</i></p> <p>The ATG discussed the concerns raised in relation to paragraph 27(a) with the AASB technical group. The AASB technical group commented that the requirement for management to understand and address estimation uncertainty is guided by the fundamental qualitative characteristics of the <i>Framework for the Preparation and Presentation of Financial Statements</i>, being relevance and faithful representation.</p> <p>Additionally, AASB 101 <i>Presentation of Financial Statements</i>, requires financial statements to present fairly the financial position, financial performance and cash flows of an entity. Furthermore, paragraph 17 of AASB 101 requires additional disclosures to be provided when compliance with the specific requirements in Australian Accounting Standards is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.</p>	

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Respondent Comment	Commentary	Change to be made to Doc? Y/N
<p><i>In relation to sub paragraph 27(b):</i></p> <ul style="list-style-type: none"> • We believe the auditor's objective is to independently challenge the reasonableness of management's work to address estimation uncertainty, as opposed to developing the estimate in cases where management's response is insufficient. • One challenge that may arise is a blurring of the lines between the auditor's and management's responsibilities with management's acceptance of the auditors' estimate over their own. A suggestion that the auditor's independence in fact or appearance may be compromised appears to be an unacceptable outcome of this requirement. Paragraph A116 recognises this potential conflict but A117 makes it clear that a modified opinion would be the outcome if the auditor cannot develop a point estimate or range. This appears to be an overly strict outcome. • In our view paragraph 27(b) should acknowledge there are other ways to gather the level of audit evidence required for an area of high estimation uncertainty, as set out under paragraph 18. • Also, it is unclear in this context what would constitute a misstatement of the estimate, and guidance would be useful. For example, it would be beneficial to clarify whether there is a presumption the auditor's estimate could be sufficiently informed such that a misstatement could be identified, posed to management and requested to be corrected. • We seek clarification about the meaning of "to the extent practicable" and suggest the inclusion of examples of instances when it is 	<p><i>Concerns in relation to paragraph 27(b):</i></p> <p>Concerns that paragraph 27(b) and related application material could lead to the auditor to assume the responsibilities of management, or otherwise raise concerns about the auditor's independence were raised at the time of the IAASB ED. The ATG's review of IAASB meeting papers on this matter notes that the requirement in paragraph 27(b), reflects the requirements contained in extant ISA 540 (paragraph 16). Additionally, while independence has always been a requirement, it has now been elevated and is now explicitly included in the standard as application material in paragraph A116. Paragraph A117 explains that where the auditor cannot develop a point estimate or range, the auditor evaluates the implications for the audit or the auditor's opinion in accordance with paragraph 34. Paragraph 34 requires that where sufficient appropriate audit evidence cannot be obtained, the auditor evaluates the implications for the audit or the auditor's opinion.</p> <p>We acknowledge some of the implementation challenges raised by KPMG and as noted in question (e) above, we aim to address these challenges through post implementation guidance for example providing guidance with reference to the terms used in paragraph 27(b) '<i>sufficiently address</i>' and '<i>extent practical</i>'. Through the Chair, the AUASB will be encouraging the IAASB in the first instance, to address</p>	

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Respondent Comment	Commentary	Change to be made to Doc? Y/N
<p>impracticable. This could be similar to the guidance in ASA 501 Audit Evidence—Specific Considerations for Inventory and Segment Information. In the absence of a clear requirement capable of consistent application, we are concerned that variability of practice will occur, with some auditors determining that independence considerations allow the development of a point estimate, and others proceeding to qualify the audit opinion.</p> <ul style="list-style-type: none"> • Additionally, we seek clarification about the meaning of “sufficiently address”, and the intended level of auditor’s discretion when applying the requirements of this paragraph. For example, where management’s estimate is deemed to be materially fairly stated, but the auditor judges that management’s process for developing the estimate did not sufficiently address estimation uncertainty, it would appear to be unnecessary to require the auditor to request management to perform additional procedures, to evaluate these, and then to develop an auditor’s point estimate or range. 	<p>these post implementation issues at a global level. These issues are not Australian specific and accordingly should be dealt with at the IAASB level. If such guidance is not developed by the IAASB, the AUASB could work on something in conjunction with other national standard setters.</p> <p><i>Compelling Reason assessment:</i></p> <p>The ATG has considered KPMG’s comments and notes that no other stakeholders have raised similar views with reference to potential compelling reason modifications.</p> <p>The compelling reasons test for modifications in the public interest is triggered where the international standard does not reflect, or is not consistent with:</p> <p>(a) The Australian regulatory arrangements; or</p> <p>(b) Principles and practices that are considered appropriate in Australia (including in the use of significant terminology).</p> <p>The criteria that have to be met before the standard is modified is contained within paragraphs 11 and 12 of <i>Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board (IAASB) and Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board (NZAuASB) (August 2014)</i>.</p>	

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
		Having considered content of the above document, the ATG does not consider there to be a compelling reason to modify the international standard.	
PwC	None noted	-	N
EY	None noted	-	N

- (c) **Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	None Noted	-	N
IPA	None Noted	-	N
ACAG	None Noted	-	N
CPA	None identified	-	N
KPMG	None identified	-	N
PwC	None noted	-	N
EY	None noted	-	N

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- (d) What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:
- (i) Where those costs are likely to occur;
 - (ii) The estimated extent of costs, in percentage terms (relative to audit fee); and
 - (iii) Whether expected costs outweigh the benefits to the users of audit services?

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	Without having undertaken an engagement under the new standard it is not possible to quantify any additional costs but the increased granularity and components of evaluating significant estimates is highly likely to lead to increased costs.	Noted	N
IPA	The IPA expects that the more comprehensive documentation requirements of the revised standard could potentially be the source of additional audit costs, however the IPA does not consider the documentation requirements unreasonable and arguably are consistent with the type of documentation that should have always been prepared.	Noted	N
ACAG	<p>ACAG expects there will be additional costs of documentation to comply with the requirements in para 39, specifically in relation to:</p> <ul style="list-style-type: none"> • how the auditor applies their professional scepticism and • assessing, evaluating and documenting the relevance and reliability of external information sources. <p>Although likely to lead to an increase in audit effort and therefore costs, ACAG believes the expanded documentation requirements will help</p>	Noted	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
	<p>ensure audit documentation is sufficiently robust to support the auditor's assessment and conclusion.</p> <p>Apart from the additional costs outlined above for the incremental effort required, ACAG does not anticipate there will be any significant costs arising from compliance with the changes to the requirements of the proposed standard.</p>		
CPA	<p>We do anticipate an increase in work effort to meet the requirements in the proposed standard, however we note that this work effort is scalable. The extent of procedures should be responsive to the level of inherent risk, being a function of estimation uncertainty, complexity, subjectivity or other inherent risk factors, and control risk, therefore it should not exceed the work necessary to obtain sufficient appropriate audit evidence.</p>	Noted	N
KPMG	<p>We expect to incur costs associated with training and coaching auditors to apply the changes in requirements. In light of the expectation that ASA 540 will increase the estimates subject to audit, the sufficiency and / or appropriateness of audit evidence to be obtained, and the documentation of the auditor's considerations, we expect costs on audits to increase. It is difficult to estimate the extent of costs or the proportion of audit fee, as each audit will be impacted in a different manner depending on the associated risks. We consider that the increase in costs will generally benefit audit quality, consistent with the intention of the AUASB and IAASB.</p> <p>However, we note that unnecessary incremental costs may be incurred where the auditor is required to comply with paragraphs 27(a) and 27(b). Firstly, the auditor may perform procedures in accordance with paragraph</p>	See comments under (b) above.	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
	27(a), and still be required to develop a point estimate or range; secondly, the only response contemplated by paragraph 27(b) is the development of a point estimate or range, which can be a costlier procedure than the alternatives in paragraph 18.		
PwC	The expectation is that due to the substantial revision of the standard there will be additional costs. It is difficult to assess the extent of the costs at this stage, but these will include initial implementation costs as well as potentially increased audit effort on some audits.	Noted	N
EY	No comments noted	-	N

- (e) **What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 540 (specific questions/examples would be helpful).**

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	The interaction between a client's point estimate and an auditor's range estimate, and the acceptable quantum of a range estimate in relation to materiality.	Paragraphs A125, A139-A144 of ED ASA 540 provides guidance in relation to this matter. The ATG will take this matter into account when post implementation guidance is considered.	N
IPA	The IPA anticipates auditor will have issues with the new expected loss model in AASB 9 <i>Financial Instruments</i> and as such believes it would be useful for implementation guidance in relation to the audit of expected	The ATG will take this matter into account when post implementation guidance is considered.	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
	<p>credit losses including the use of the provision matrix approach under the simplified approach.</p> <p>The other area the IPA believes implementation guidance would be useful is in relation to impairment testing particularly when fair values less cost of disposal is used.</p>		
ACAG	<p>ACAG would like the AUASB to issue, in conjunction with the release of ASA 540, implementation guidance to provide clarity on the auditor's point estimate, the auditor's range and the multiples of materiality, specifically:</p> <ul style="list-style-type: none"> • when it would be appropriate for the auditor to develop a point estimate instead of a range and • the application of multiples of materiality and the how this interrelates to the identification of a misstatement. <p>ACAG believes it would be useful for the AUASB to provide additional guidance to help auditors determine when it is not 'practicable' to develop a point estimate or range, as this term is not within the extant standard.</p>	The ATG will take these matters into account when post implementation guidance is considered.	N
CPA	<p>Some assistance by way of implementation guidance or technical Q&A would be helpful. In particular, using examples which demonstrate:</p> <p>The work effort required for less complex estimates, even if they are very material, in contrast to estimates with a high level of estimation uncertainty, which are complex and subjective.</p>	The ATG will take these matters into account when post implementation guidance is considered.	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
	<p>Whether significant risks include estimates on the extremes of the spectrum of inherent risk, that is, those which are material but not complex or not as material but highly complex.</p> <p>Diagrams and flowcharts of the decision-making process followed to arrive at the nature and extent of audit procedures required for different types of estimates could also be helpful.</p>		
KPMG	<p>In our view it would be beneficial for the AUASB to consider issuing guidance similar to that included in PCAOB Release No. 2017-002 issued 1 June 2017 in relation to:</p> <ul style="list-style-type: none"> • Examples of Use of Pricing Information from Third Parties and Audit Evidence; and • Audit Evidence Regarding Valuation of Investments Based on Investee Financial Condition or Operating Results. <p>The proposed inclusions in AS 2501 Auditing Accounting Estimates, Including Fair Value Measurements and AS 1105 Audit Evidence respectively, provide guidance on two aspects of estimation complexity that Australian auditors would find relevant and useful in interpreting and applying ASA 540.</p>	The ATG will take these matters into account when post implementation guidance is considered.	N
PwC	We believe that additional guidance on the expected information and documentation under the new standard for those responsible for the accounting estimate and disclosures would be beneficial.	The ATG will take these matters into account when post implementation guidance is considered.	
EY	No comments noted	-	N

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- (f) **The AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:**

Paragraphs 27: *Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty*

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	It is unclear how or why the auditor would conclude that management had not taken sufficient steps with regard to estimation uncertainty if their estimate was within the auditor's acceptable range.	Paragraph A109 provides guidance as to relevant considerations regarding whether management has taken appropriate steps to understand and address estimation uncertainty.	N
IPA	The IPA does not find the guidance in relation to ASA 540.27 particularly useful. The guidance is vague and does not provide a clear course of action for the auditor. Furthermore, the guidance barely deals with disclosure issues.	The ATG considers that the guidance under paragraphs A115-A117 provides a clear course of action for the auditor.	N
ACAG	ACAG is supportive of the enhanced requirements on what further audit procedures are required when management has not taken the appropriate steps to address estimation uncertainty and agrees with the guidance in para A116 that in doing so, the auditor should ensure independence requirements are not compromised. ACAG believes it would be useful for the AUASB to provide additional guidance to help auditors determine when it is not 'practicable' to develop a point estimate or range, as this term is not within the extant standard.	The ATG will take the suggestion into account when post implementation guidance is considered.	N
CPA	We are supportive of the inclusion in this requirement for a request to management to perform additional procedures if they have not properly understood or addressed estimation uncertainty. Then only if management's response is insufficient, is the auditor expected to develop their own point	-	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
	estimate or range. This is a more reasonable process than that proposed in the earlier IAASB exposure draft.		
KPMG	See b above.	See b above	N
PwC	We believe that the matters raised by the AUASB have been addressed in the standard and support that the standard requires the appropriate level of professional scepticism.	-	N
EY	The Director's responsibility in relation to the preparation and fair presentation of the financial report include the responsibilities to address estimation uncertainties by selecting an appropriate point estimates and by developing related disclosures about estimation uncertainties. We are supportive of distinguishing this responsibility in ED-03/18 in the definition of the Auditor's point estimate or auditor's range as one developed in evaluating management's point estimate and requirement in paragraph 27(a) to request management to perform additional procedures.	-	N

- (g) **The AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:**

Paragraphs 30: *Other Considerations Relating to Audit Evidence*

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	None Noted	-	N
IPA	None Noted	-	N
ACAG	ACAG agrees with the requirements in para 30 as they are broadly consistent with the requirements in paras 8(c) and A48 of the extant ASA 500 Audit Evidence. ACAG believes the insertion of para 30 crystalizes the requirements to evaluate the expert's work as audit evidence, which may not have been sufficiently performed and documented previously.	-	N
CPA	We are supportive of the additional requirements which link to ASA 500, including for evaluation of management's experts work.	-	N
KPMG	We are concerned that paragraph 30 together with A130 and A131 require the auditor to request a management expert to comply with paragraph 27 and could be difficult to enforce in practice. As above, without an equivalent requirement on the management expert, in our view paragraph 27(a) is essentially redundant and the likely outcome is that the auditor will default to paragraph 27(b).	From the ATG's review of the basis of conclusions behind the final ISA 540, the ATG note that it is not the IAASB's intention that the auditor addresses every single requirement in paragraphs 21-29 when using the work of a management's expert but that the auditor may consider the matters described in paragraphs 21-29 in complying with the existing requirements of paragraph 8(c) of ASA 500 as referred to in A131.	N
PwC	We believe that the matters raised by the AUASB have been addressed in the standard and support that the standard requires the appropriate level of professional scepticism.	-	N
EY	None noted	-	N

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- (h) **The AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:**

Paragraph 33: *Overall Evaluation Based on Audit Procedures Performed*

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	The paragraph appears redundant as considering the evidence and its sufficiency as part of assessing the entire body of audit work therefore why is it expressly called out for estimates.	The IAASB's Basis of Conclusions notes that inspection findings raise significant concerns about audit quality for accounting estimates, and a need to address this by fostering a more independent and challenging sceptical mindset in auditors. The IAASB considers that the placement of the stand back provision in ED ASA 540 will foster improved application of professional scepticism.	N
IPA	The IPA does not believe ASA 540.33 and related guidance adequately address the issue of an overall evaluation of an accounting estimate in terms of the macro-economic environment, the industry and the client's capabilities.	The guidance in paragraph A137 links through to the risk assessment procedures where these factors would ordinarily be considered.	N
ACAG	ACAG agrees with the requirements in para 33 as they are broadly consistent with the requirements in paras 25-26 of the extant ASA 330 <i>The Auditor's Response to Assessed Risks</i> . ACAG believes that although 'stand back' is likely to be performed in practice, the explicit requirement to do so, will help ensure the documentation supports the auditor's assessment.	-	N
CPA	We are supportive of this requirement to "stand back" and make an overall evaluation of accounting estimates.	-	N
KPMG	No further comments - supportive	-	N

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
PwC	We believe that the matters raised by the AUASB have been addressed in the standard and support that the standard requires the appropriate level of professional scepticism.	-	N
EY	<ul style="list-style-type: none"> We support the consideration of all relevant audit evidence, whether corroborative or contradictory, as required in paragraph 34 of ED-03/18. However, we believe the last sentence of paragraph 34 appears to be misplaced because it addresses the implications of the auditor not obtaining sufficient appropriate audit evidence. These implications seem to be more closely related to evaluations performed in paragraph 33(a) and 33(b) of ED-03/18. We do not believe the determination of whether disclosures beyond those required by the financial reporting framework, which is currently included in paragraph 36 of ED-03/18, should be included in the requirements. Including this evaluation in the requirements, in our view, de-emphasizes the importance of the auditor's evaluation of whether the disclosures are in accordance with the requirements of the financial reporting framework, which we believe is challenging in itself. <p>Because paragraphs 13 and 14 of ASA 700 (Revised) address the auditor's evaluation of fair presentation of the financial statements, including the disclosures, we believe it would be more appropriate for the application material in ED-03/18 to address and explain the relationship of the required overall evaluation of estimates and related disclosures to the evaluation of fair presentation in ASA 700 (Revised). In this regard, we believe such application material would be best</p>	<ul style="list-style-type: none"> The ATG considers that the placement of this last sentence of paragraph 34, is appropriately linked to the whole of paragraph 33. While ASA 700 essentially contains an overall stand-back in relation to overall fair presentation, the IAASB in all open projects, is introducing these stand-back provisions. The Basis of Conclusions notes that inspection findings raise significant concerns about audit quality for accounting estimates, and a need to address this by fostering a more independent and challenging sceptical mindset in auditors. The IAASB considers that the placement of the stand back provision in ED ASA 540 will foster improved application of professional scepticism. 	

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Respondent Comment		Commentary	Change to be made to Doc? Y/N
	placed in support of the overall evaluation in paragraph 35 of ED-03/18.		

(i) Are there any other significant public interest matters that stakeholders wish to raise?

Respondent Comment		Commentary	Change to be made to Doc? Y/N
R1	None Noted	-	N
IPA	None Noted	-	N
ACAG	Overall, ACAG is supportive of the proposed standard. We believe the additional application guidance and worked examples referred above would help auditors comply with the requirements of ASA 540.	The ATG will take these matters into account when post implementation guidance is considered.	N
CPA	We do not wish to raise any public interest matters.	-	N
KPMG	No further comments	-	N
PwC	None noted	-	N

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EXHIBIT 2 – OTHER GENERAL COMMENTS

Item No.	Ref Para No.	Respondent Comment		Commentary	Change to be made to Doc? Y/N
1		IPA	Inherent Bias – the standard manifests an inherent bias towards consistency in assumptions and basis of estimates. It is the IPA's contention that audit failure is often a result of accepting the estimate based on consistency with prior years when in fact the assumptions should change regularly. Risk-free rates, WACC, growth rates among other assumptions should change yearly with changes in the macro-economic conditions, industry and client specific factors.	There are several requirements (paragraphs 23(a), 24(a), 25(a)) and guidance (paragraph A95) that specifically address changes from prior years in relation to methods, assumptions and data.	N
2		IPA	Management Bias – The IPA does not believe management bias is properly dealt with. The focus is on evidence of management bias in the determination of accounting estimates in particular the selection of assumptions. The IPA is of the view the standard should acknowledge that inherent risk related to a motive to misstate by management arising from factors such as remuneration arrangements. The IPA believes such inherent risk should affect the nature, extent and timing of audit procedures carried out in relation to accounting estimates and the current structure of ASA 540 does not adequately address such considerations.	The ATG considers that management bias is considered extensively throughout the standard. The standard has specific requirements in relation to management bias considerations in respect of methods, assumptions and data (paragraphs 23(b), 24(b), 25(b)), as well as considering indicators of possible management bias (paragraph 32). Additionally, there is extensive application material (paragraphs A96, A133-A135). There is also application material linking ASA 540 to ASA 240 in relation to management bias and fraud.	N

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Item No.	Ref Para No.	Respondent Comment		Commentary	Change to be made to Doc? Y/N
3		IPA	Disclosures – currently the quality of disclosures in relation to estimation uncertainty and management judgements are variable and some of the responsibility lays with auditors not sufficiently understanding their obligations in regard to such disclosures. ASA 540 while it does acknowledge these obligations, it does not provide much guidance in this area. The IPA believes ASA 540 should include more comprehensive guidance in relation to the audit of disclosures relating to estimation uncertainty and management judgements including the application of materiality to such disclosures.	The ATG will take into account when post implementation guidance is considered	N
4		IPA	Quality of Application Guidance – The IPA is disappointed that the application guidance included in ASA 540 is mainly in the nature of explanatory material and does not provide much in the way of practical guidance. In addition, the guidance is often not definitive and in essence requires the exercise of auditor judgement.	The ASAs are a set of principles-based standards characterised by the exercise of auditor's professional judgement, meaning that the standards should be able to deal with evolving business environments and financial reporting frameworks. As noted by question (e) above, the intention of the AUASB is to work through what post implementation guidance is required by stakeholders.	N

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Item No.	Ref Para No.	Respondent Comment		Commentary	Change to be made to Doc? Y/N
5		EY	We are concerned about changing the criterion for the auditor's evaluation of disclosures related to accounting estimates to "reasonable" from "adequate". Although we conceptually agree with the explanation provided in paragraph 9, we believe such a definition leads to the need for the AUASB to further consider whether the term "reasonable" should be replaced with the clearer terminology in the context of disclosures about the accounting estimates.	<p>The ATG has reviewed the IAASB's Basis for Conclusions and notes that the IAASB recognises a degree of inconsistency in the language of the standards but decided not to make conforming amendments at this time, but rather to consider the need for such amendments, as part of the post-implementation review of the auditor reporting standards. ED ASA 540 paragraphs A12-A13 does provide an explanation of reasonable and how this relates to appropriate.</p> <p>The ATG could consider whether post implementation guidance in relation to this matter would be helpful.</p>	N

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Item No.	Ref Para No.	Respondent Comment	Commentary	Change to be made to Doc? Y/N
		<p>Implications for the auditor's evaluation of misstatements in disclosures - Paragraphs A17 of ASA 450, and A3 and A7 of ASA 705 (Revised) guide the auditor in evaluating whether misstatements in disclosures are material. This guidance, referenced in ED-03/18 in paragraph A142, speaks to the appropriateness, accuracy and adequacy of disclosures, and it is unclear how the AUASB's proposed change in ED-03/18 to evaluate their "reasonableness" affects the auditor's evaluation of material misstatements in accordance with ASA 450. This disparity in terminology runs the risk of the auditor making inappropriate judgments about whether the financial statements are materially misstated. As expressed, we believe the terminology for evaluation of disclosures, if changes are pursued in conjunction with ED-03/18, needs to be aligned across the ASAs, in particular across ED-03/18, ASA 450, ASA 700 (Revised) and ASA 705 (Revised). Accordingly, additional guidance is required to support the conforming amendment proposed to paragraph 13 (c) to read "the accounting estimates and related disclosures are reasonable".</p>		

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INSTITUTE OF
**PUBLIC
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IPA Submission

**Exposure Draft ED03/18 *ASA 540 Auditing Accounting
Estimates and Related Disclosures***

16 October 2018

15 October 2018

Mr Roger Simmett
The Chair and CEO
Australian Auditing and Assurance Board
PO Box 204 Collins Street West
Melbourne VIC 8007

Dear Roger

**Re: Exposure Draft ED03/18 ASA 540 Auditing Accounting Estimates and
Related Disclosures**

On behalf of the Institute of Public Accountants (IPA), I submit our review of Exposure Draft ED 3/18 *ASA 540 Auditing Accounting Estimates and Related Disclosures*.

The IPA broadly supports the revisions to ASA 540. However, the IPA is of the view that the revised ASA 540 should have better addressed the following issues:

1. Overall Assessment of Estimate – the standard is focused on the components that constitute an accounting estimate but does not place enough emphasis on the overall outcome of the estimation process. The standard needs to provide better guidance in relation to the review of the outcomes in the context of macro-economic, industry and client constraints when auditing the appropriateness of accounting estimates.
2. Inherent Bias – the standard manifests an inherent bias towards consistency in assumptions and basis of estimates. It is the IPA's contention that audit failure is often a result of accepting the estimate based on consistency with prior years when in fact the assumptions should change regularly. Risk-free rates, WACC, growth rates among other assumptions should change yearly with changes in the macro-economic conditions, industry and client specific factors.
3. Management Bias – The IPA does not believe management bias is properly dealt with. The focus is on evidence of management bias in the determination of accounting estimates in particular the selection of assumptions. The IPA is of the view the standard should acknowledge that inherent risk related to a motive to misstate by management arising from factors such as remuneration arrangements. The IPA believes such inherent risk should affect the nature, extent and timing of audit procedures carried out in relation to accounting estimates and the current structure of ASA 540 does not adequately address such considerations.
4. Disclosures – currently the quality of disclosures in relation to estimation uncertainty and management judgements are variable and some of the responsibility lays with auditors not sufficiently understanding their obligations in regard to such disclosures. ASA 540 while it does acknowledge these obligations, it does not provide much guidance in this area. The IPA believes ASA 540 should include more comprehensive guidance in relation to the audit of disclosures relating to estimation uncertainty and management judgements including the application of materiality to such disclosures.

5. Quality of Application Guidance – The IPA is disappointed that the application guidance included in ASA 540 is mainly in the nature of explanatory material and does not provide much in the way of practical guidance. In addition, the guidance is often not definitive and in essence requires the exercise of auditor judgement.

Our comments and responses to the questions in the Exposure Draft are set out in the Appendix to this letter.

If you would like to discuss our comments, please contact me or our technical advisers Mr Stephen LaGreca (stephenlagreca@aol.com) or Mr Colin Parker (colin@gaap.com.au) (a former member of the AASB), GAAP Consulting.

Yours sincerely

Vicki Stylianou
Executive General Manager, Advocacy & Technical
Institute of Public Accountants

About the IPA

The IPA is a professional organisation for accountants recognised for their practical, hands-on skills and a broad understanding of the total business environment. Representing more than 35,000 members in Australia and in over 65 countries, the IPA represents members and students working in industry, commerce, government, academia and private practice. Through representation on special interest groups, the IPA ensures the views of its members are voiced with government and key industry sectors and makes representations to Government including the Australian Tax Office (ATO), Australian Securities and Investments Commission (ASIC) and the Australian Prudential Regulation Authority (APRA) on issues affecting our members, the profession and the public interest. The IPA recently merged with the Institute of Financial Accountants of the UK, making the new IPA Group the largest accounting body in the SMP/SME sector in the world.

Appendix

Question 1

Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

IPA response

The IPA is not aware of any reference to law or regulation that has been omitted from the proposed revised standard.

Question 2

Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

IPA response

The IPA is unaware of any law or regulation that would impede the application of the proposed standard.

Question 3

Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

IPA response

The IPA is unaware of any principle or practice that may impede or conflict with the proposed standard.

Question 4

What, if any are the additional significant costs to /benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

- (a) Where those costs are likely to occur;*
- (b) The estimated extent of costs, in percentage terms (relative to audit fee);*
and
- (c) Whether expected costs outweigh the benefits to the users of audit services?*

IPA response

The IPA expects that the more comprehensive documentation requirements of the revised standard could potentially be the source of additional audit costs, however the IPA does not consider the documentation requirements unreasonable and arguably are consistent with the type of documentation that should have always been prepared.

Question 5

What, if any implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ISA 540 (specific questions/examples would be helpful).

IPA response

The IPA anticipates auditor will have issues with the new expected loss model in AASB 9 *Financial Instruments* and as such believes it would be useful for implementation guidance in relation to the audit of expected credit losses including the use of the provision matrix approach under the simplified approach.

The other area the IPA believes implementation guidance would be useful is in relation to impairment testing particularly when fair values less cost of disposal is used.

Question 6

Over the course of the development of the IAASB's ISA 540, the AUASB discussed a number of issues that were raised by Australian stakeholders at various feedback sessions. The AUASB provided feedback on these matters directly to the IAASB. The IAASB has sought to address these issues in the development of the final ISA 540 that the AUASB now exposes as ED 03/18. Accordingly, the AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:

- (d) Paragraph 27: Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty*
- (e) Paragraph 30: Other Considerations Relating to Audit Evidence*
- (f) Paragraph 33: Overall Evaluation Based on Audit Procedures Performed*

IPA response

(d) The IPA does not find the guidance in relation to ISA 540.27 (ISA 540.A115-A117) particularly useful. The guidance is vague and does not provide a clear course of action for the auditor. Furthermore, the guidance barely deals with disclosure issues.

(e) The IPA has no comment on ISA 540.30 and related guidance (ISA 540.A126-A132).

(f) The IPA does not believe ASA 540.33 and related guidance ASA 540.A137-A138, ASA 540.34-36 and ASA 540.A139-A144 adequately address the issue of an overall evaluation of an accounting estimate in terms of the macro-economic environment, the industry and the client's capabilities.

Question 7

Are there any other significant public interest matters that stakeholders wish to raise?

IPA Response

The IPA has no other public interest matters it wishes to raise other than the matters included in the covering letter.



15 October 2018

The Chair
Australian Auditing and Assurance Standards Board
PO Box 204
Collins St West Victoria 8007
AUSTRALIA

Dear Professor Simnett

Request for Comment

ED 03/18 Proposed Auditing Standard ASA 540 Auditing Accounting Estimates and Related Disclosures and

ED 04/18 Proposed Auditing Standard ASA 2018 -2 Amendments to Australian Auditing Standards

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to comment on exposure drafts 03/18 *Proposed Auditing Standard ASA 540 Auditing Accounting Estimates and Related Disclosures* and 04/18 *Proposed Auditing Standard ASA 2018 -2 Amendments to Australian Auditing Standards*. The views expressed in this submission represent those of all Australian members of ACAG.

ACAG's comments are primarily in the context of the public sector, which reflects ACAG's significant experience and involvement in the sector.

Overall ACAG agrees with the changes within ED 03/18 and ED 04/18 and acknowledge that the proposed standards have incorporated the main concerns raised by respondents from the original exposure draft. We have, however, identified some areas where we believe the AUASB should consider providing guidance to help operationalise and ensure compliance with, the requirements within the proposed standard.

ACAG appreciates the opportunity to comment and trust that you will find the attached comments useful.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Richardson', with a stylized flourish at the end.

Andrew Richardson
Chairman
ACAG Audit Standards Committee

ATTACHMENT

Specific Matters for Comment

ED 03/18: Proposed Auditing Standard ASA 540 *Auditing Accounting Estimates and Related Disclosures*

1. Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

ACAG makes no comment on this matter.

2. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

ACAG is not aware of any such laws and regulations.

3. Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

ACAG does not believe there are principles or practices that prevent or impede the application of, or conflict with, the proposed standard.

4. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

- (a) Where those costs are likely to occur, compliance costs?**
- (b) The estimated extent of costs, in percentage terms (relative to audit fee); and**
- (c) Whether expected costs outweigh the benefits to the users of audit services?**

ACAG expects there will be additional costs of documentation to comply with the requirements in para 39, specifically in relation to:

- how the auditor applies their professional scepticism and
- assessing, evaluating and documenting the relevance and reliability of external information sources.

Although likely to lead to an increase in audit effort and therefore costs, ACAG believes the expanded documentation requirements will help ensure audit documentation is sufficiently robust to support the auditor's assessment and conclusion.

Apart from the additional costs outlined above for the incremental effort required, ACAG does not anticipate there will be any significant costs arising from compliance with the changes to the requirements of the proposed standard.

5. What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 540 (specific questions/examples would be helpful).

ACAG would like the AUASB to issue, in conjunction with the release of ASA 540, implementation guidance to provide clarity on the auditor's point estimate, the auditor's range and the multiples of materiality, specifically:

- when it would be appropriate for the auditor to develop a point estimate instead of a range and
- the application of multiples of materiality and the how this interrelates to the identification of a misstatement.

6. Over the course of the development of the IAASB's ISA 540, the AUASB discussed a number of issues that were raised by Australian stakeholders at various feedback sessions. The AUASB provided feedback on these matters directly to the IAASB. The IAASB has sought to address these issues in the development of the final ISA 540 that the AUASB now exposes as ED 03/18. Accordingly, the AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:

(a) Paragraph 27: Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty

ACAG is supportive of the enhanced requirements on what further audit procedures are required when management has not taken the appropriate steps to address estimation uncertainty, and agrees with the guidance in para A116 that in doing so, the auditor should ensure independence requirements are not compromised.

ACAG believes it would be useful for the AUASB to provide additional guidance to help auditors determine when it is not 'practicable' to develop a point estimate or range, as this term is not within the extant standard.

(b) Paragraph 30: Other Considerations Relating to Audit Evidence

ACAG agrees with the requirements in para 30 as they are broadly consistent with the requirements in paras 8(c) and A48 of the extant ASA 500 *Audit Evidence*. ACAG believes the insertion of para 30 crystalizes the requirements to evaluate the expert’s work as audit evidence, which may not have been sufficiently performed and documented previously.

(c) Paragraph 33: Overall Evaluation Based on Audit Procedures Performed

ACAG agrees with the requirements in para 33 as they are broadly consistent with the requirements in paras 25-26 of the extant ASA 330 *The Auditor’s Response to Assessed Risks*. ACAG believes that although ‘stand back’ is likely to be performed in practice, the explicit requirement to do so, will help ensure the documentation supports the auditor’s assessment.

7. Are there any other significant public interest matters that stakeholders wish to raise?

The AUASB prefers that respondents express a clear opinion on whether the proposed Auditing Standard, as a whole, is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the above matters. The AUASB regards both supportive and critical comments as essential to a balanced review of the proposed Auditing Standard.

Overall, ACAG is supportive of the proposed standard. We believe the additional application guidance and worked examples referred above would help auditors comply with the requirements of ASA 540.

Specific Matters for Comment

ED 04/18: Proposed Auditing Standard ASA 2018-2 *Amendments to Australian Auditing Standards*

1. Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

ACAG makes no comment on this matter.

2. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

ACAG is not aware of any such laws and regulations.

3. Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

Overall, ACAG does not believe there are principles or practices that may or do prevent or impede the application of, or conflict with the proposed standard. However, we highlight the following references in the proposed amendments which do not appear to be consistent with requirements in the proposed ASA 540:

- para 7 (ASA 200) refers to 'ASA 540....para 15' which we believe should be 'ASA 540....para 16'
- para 10 (ASA 230) refers to 'ASA 540....para 37' which we believe should be 'ASA 540....para 39'
- para 15 (ASA 260) refers to 'ASA 540...para 36' which we believe should be 'ASA 540....38'
- para 45 (ASA 701) refers to 'ASA 540....para 15' which we believe should be 'ASA 540....16(a)'.

In addition to the above, the amendments proposed to:

- a) ASA 240 in paras 11-12 do not appear to be correct:
 - para 11 refers to 'Existing para A48' which we believe should be 'Existing para A47'
 - para 12 refers to 'Existing footnote 20' which we believe should be 'Existing footnote 18'.
- b) ASA 500 in para 33 do not appear to be correct:
 - 'See ASA 330, para 6' which we believe should be 'See ASA 330, para 7'
 - 'See ASA 540, para 29' which we believe should be 'See ASA 540, para 30'.

In relation to the proposals to extant ASA 500, ACAG recommends the inclusion of an introductory sentence that links the concept of 'information obtained from other sources' within extant 5c) to the proposed definition of 'external information source'.

4. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

- (a) Where those costs are likely to occur;**
- (b) The estimated extent of costs, in percentage terms (relative to audit fee); and**
- (c) Whether expected costs outweigh the benefits to the users of audit services?**

Apart from the additional costs outlined below for the incremental effort required, ACAG does not anticipate there will be any significant costs arising from compliance with the changes to the requirements of the proposed standard.

ACAG expects there will be additional costs of documentation to comply with the requirements in para 39, specifically in relation to:

- how the auditor applies their professional scepticism and
- assessing, evaluating and documenting the relevance and reliability of external information sources.

Although likely to lead to an increase in audit effort and therefore costs, ACAG believes the expanded documentation requirements will help ensure audit documentation is sufficiently robust to support the auditor's assessment and conclusion.

5. Are there any other significant public interest matters that stakeholders wish to raise?

ACAG is not aware of any other significant public interest matters.

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15 October 2018

Prof Roger Simnett
The Chair
Auditing and Assurance Standards Board
PO Box 204, Collins St West
Melbourne, VIC 8007
Australia

On-line submission: www.auasb.gov.au/Work-In-Progress/Open-for-comment.aspx

Dear Roger

Submission on Exposure Draft ED 03/18 Proposed Auditing Standard ASA 540 *Auditing Accounting Estimates and Related Disclosures*

CPA Australia represents the diverse interests of more than 163,000 members working in 125 countries and regions around the world. We make this submission on behalf of our members and in the broader public interest.

CPA Australia supports the proposed auditing standard ASA 540 *Auditing Accounting Estimates and Related Disclosures*, as we consider that it addresses the need for a more robust audit approach for complex estimates whilst still allowing for a proportionate scalable audit response to less complex estimates.

Consultation questions and responses

1. **Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?**

No omissions noted.

2. **Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

None identified.

3. **Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

None identified.

4. **What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand: (a) Where those costs are likely to occur;**

(b) The estimated extent of costs, in percentage terms (relative to audit fee); and

(c) Whether expected costs outweigh the benefits to the users of audit services?

We do anticipate an increase in work effort to meet the requirements in the proposed standard, however we note that this work effort is scalable. The extent of procedures should be responsive to the level of inherent risk, being a function of estimation uncertainty, complexity, subjectivity or other inherent risk factors, and control risk, therefore it should not exceed the work necessary to obtain sufficient appropriate audit evidence.

5. What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ISA 540 (specific questions/examples would be helpful).

Some assistance by way of implementation guidance or technical Q&A would be helpful. In particular, using examples which demonstrate:

- The work effort required for less complex estimates, even if they are very material, in contrast to estimates with a high level of estimation uncertainty, which are complex and subjective.
- Whether significant risks include estimates on the extremes of the spectrum of inherent risk, that is, those which are material but not complex or not as material but highly complex.

Diagrams and flowcharts of the decision making process followed to arrive at the nature and extent of audit procedures required for different types of estimates could also be helpful.

6. Over the course of the development of the IAASB's ISA 540, the AUASB discussed a number of issues that were raised by Australian stakeholders at various feedback sessions. The AUASB provided feedback on these matters directly to the IAASB. The IAASB has sought to address these issues in the development of the final ISA 540 that the AUASB now exposes as ED 03/18. Accordingly the AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:

(a) Paragraph 27: Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty

We are supportive of the inclusion in this requirement for a request to management to perform additional procedures if they have not properly understood or addressed estimation uncertainty. Then only if management's response is insufficient, is the auditor expected to develop their own point estimate or range. This is a more reasonable process than that proposed in the earlier IAASB exposure draft.

(b) Paragraph 30: Other Considerations Relating to Audit Evidence

We are supportive of the additional requirements which link to ISA 500, including for evaluation of management's experts work.

(c) Paragraph 33: Overall Evaluation Based on Audit Procedures Performed

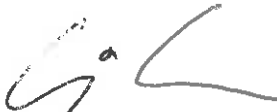
We are supportive of this requirement to "stand back" and make an overall evaluation of accounting estimates.

7. Are there any other significant public interest matters that stakeholders wish to raise?

We do not wish to raise any public interest matters.

If you require further information on our views expressed in this submission, please contact Claire Grayston, Policy Adviser – Audit & Assurance, on +61 3 9606 5183 or at claire.grayston@cpaaustralia.com.au.

Yours sincerely

A handwritten signature in black ink, appearing to be 'CL' or similar, written over a light gray circular stamp.

Craig Laughton

Executive General Manager Policy, Advocacy & Public Practice



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The Chair
Auditing and Assurance Standards Board
PO Box 204
Collins Street West
Melbourne Victoria 8007

Our ref ED comment submission ASA
540
Contact Juliet Low (+61 2 9295 3881)

15 October 2018

Dear Sir,

Comment submission on AUASB Exposure Draft (ED) ASA 540 *Auditing Accounting Estimates and Related Disclosures*

We are pleased to have the opportunity to respond to ASA 540 *Auditing Accounting Estimates and Related Disclosures* ED issued by the Australian Auditing and Assurance Standards Board (AUASB). This letter represents the views of KPMG Australia.

Overall, KPMG Australia is supportive of the adoption of the proposed Auditing Standard.

Please refer to Appendix 1 to this letter for our views and responses to the specific questions raised by the AUASB for comment.

Should you wish to clarify any aspect of KPMG Australia's submission, I would be pleased to discuss. My contact details are julietlow@kpmg.com.au or (02) 9295 3881.

Yours faithfully,

A handwritten signature in blue ink that reads 'Juliet Low'.

Juliet Low
Partner

Appendix 1 – KPMG Australia’s views on specific matters highlighted by AUASB in the Exposure Draft (ED) ASA 540 Auditing Accounting Estimates and Related Disclosures

1. Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?

We believe the applicable laws and regulations have been appropriately addressed and no references to relevant laws or regulations have been omitted.

2. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

A blurring of the lines between the auditor’s and management’s responsibilities could occur where the auditor is required by paragraph 27(b) to develop a point estimate or range. This may conflict with legal requirements for the auditor to be independent in fact and appearance. Paragraph A116 refers to this possibility. However, the standard currently leads to a modified opinion if the auditor cannot develop a point estimate or range without compromising independence. A more proportionate outcome could be obtained if paragraph 27(b) was amended – refer to point 6 below.

Other than this, we do not believe any applicable laws and regulations may impact or conflict with the proposed standard.

3. Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

We are not aware of any relevant principles and practices that may impact the application of the proposed standard.

4. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:

- (a) Where those costs are likely to occur;***
- (b) The estimated extent of costs, in percentage terms (relative to audit fee); and***
- (c) Whether expected costs outweigh the benefits to the users of audit services?***

We expect to incur costs associated with training and coaching auditors to apply the changes in requirements. In light of the expectation that ASA 540 will increase the estimates subject to audit, the sufficiency and / or appropriateness of audit evidence to be obtained, and the documentation of the auditor's considerations, we expect costs on audits to increase. It is difficult to estimate the extent of costs or the proportion of audit fee, as each audit will be impacted in a different manner depending on the associated risks. We consider that the increase in costs will generally benefit audit quality, consistent with the intention of the AUASB and IAASB.

However, we note that unnecessary incremental costs may be incurred where the auditor is required to comply with paragraphs 27(a) and 27(b). Firstly, the auditor may perform procedures in accordance with paragraph 27(a), and still be required to develop a point estimate or range; secondly, the only response contemplated by paragraph 27(b) is the development of a point estimate or range, which can be a more costly procedure than the alternatives in paragraph 18.

5. What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 540 (specific questions/examples would be helpful).

In our view it would be beneficial for the AUASB to consider issuing guidance similar to that included in PCAOB Release No. 2017-002 issued 1 June 2017 in relation to:

- Examples of Use of Pricing Information from Third Parties and Audit Evidence; and
- Audit Evidence Regarding Valuation of Investments Based on Investee Financial Condition or Operating Results.

The proposed inclusions in AS 2501 *Auditing Accounting Estimates, Including Fair Value Measurements* and AS 1105 *Audit Evidence* respectively, provide guidance on two aspects of estimation complexity that Australian auditors would find relevant and useful in interpreting and applying ASA 540.

6. Specific stakeholder feedback requested:

Paragraph 27: Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty

As set out below, we have significant concerns with paragraph 27(b), which prescribes one specific response to circumstances outside the auditor's control, over and above additional procedures required by paragraph 27(a).

In relation to sub paragraph 27 (a):

While subparagraph 27 (a) emphasises the importance of management's responsibility to perform the necessary procedures to understand and address estimation uncertainty, we have the following concerns:

- We have reservations about the effectiveness of this requirement because management, as the preparers of financial statements including estimates, are not

obliged to comply with auditing standards but with accounting standards. The requirement for management to understand and address estimation uncertainty does not currently reside within the accounting standards. Thus the requirement on the auditor to request “management to perform additional procedures to understand estimation uncertainty or to address it” is not backed by a similar obligation on the preparer. We recommend the AUASB engage in discussions with the AASB to insert a similar requirement to the same effect within the accounting standards.

- Without an equivalent requirement on management, paragraph 27(a) is essentially redundant and requires an additional work effort from the auditor which could be avoided by defaulting to paragraph 27(b).

In relation to sub paragraph 27(b):

- We believe the auditor’s objective is to independently challenge the reasonableness of management’s work to address estimation uncertainty, as opposed to developing the estimate in cases where management’s response is insufficient.
- One challenge that may arise is a blurring of the lines between the auditor’s and management’s responsibilities with management’s acceptance of the auditors’ estimate over their own. A suggestion that the auditor’s independence in fact or appearance may be compromised appears to be an unacceptable outcome of this requirement.
- Paragraph A116 recognises this potential conflict but A117 makes it clear that a modified opinion would be the outcome if the auditor cannot develop a point estimate or range. This appears to be an overly strict outcome.
- In our view paragraph 27(b) should acknowledge there are other ways to gather the level of audit evidence required for an area of high estimation uncertainty, as set out under paragraph 18.
- Also, it is unclear in this context what would constitute a misstatement of the estimate, and guidance would be useful. For example, it would be beneficial to clarify whether there is a presumption the auditor’s estimate could be sufficiently informed such that a misstatement could be identified, posed to management and requested to be corrected.
- We seek clarification about the meaning of “to the extent practicable” and suggest the inclusion of examples of instances when it is impracticable. This could be similar to the guidance in ASA 501 *Audit Evidence—Specific Considerations for Inventory and Segment Information*. In the absence of a clear requirement capable of consistent application, we are concerned that variability of practice will occur, with some auditors determining that independence considerations allow the development of a point estimate, and others proceeding to qualify the audit opinion.
- Additionally, we seek clarification about the meaning of “sufficiently address”, and the intended level of auditor’s discretion when applying the requirements of this

paragraph. For example, where management's estimate is deemed to be materially fairly stated, but the auditor judges that management's process for developing the estimate did not sufficiently address estimation uncertainty, it would appear to be unnecessary to require the auditor to request management to perform additional procedures, to evaluate these, and then to develop an auditor's point estimate or range.

We have no comments in relation to sub paragraph 27 (c).

Paragraph 30: Other Considerations Relating to Audit Evidence

We are concerned that paragraph 30 together with A130 and A131 require the auditor to request a management expert to comply with paragraph 27, and could be difficult to enforce in practice. As above, without an equivalent requirement on the management expert, in our view paragraph 27(a) is essentially redundant and the likely outcome is that the auditor will default to paragraph 27(b).

Paragraph 33: Overall Evaluation Based on Audit Procedures Performed

We are supportive of the requirements in paragraph 33 and have no further comments.

7. Are there any other significant public interest matters that stakeholders wish to raise?

No, there are no other significant public interest matters we wish to raise.

The Chair
Auditing and Assurance Standards Board
PO Box 204
Collins Street West
Melbourne VIC 8007

16 October 2018

Dear Prof Simnett

Exposure Draft 03/18: Proposed Auditing Standard ASA 540 *Auditing Accounting Estimates and Related Disclosures*

We appreciate the opportunity to comment on the above mentioned Exposure Draft.

We support the proposed standard and the AUASB's policy to only amend the ISAs when there are compelling reasons to do so.

We have included our responses to the specific questions included in the Request for Comment in the Appendix to this letter.

We would be pleased to discuss our comments with you. Please contact me on (03) 8603 3285 should you require any further information.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Valerie Clifford', with a stylized flourish at the end.

Valerie Clifford
Assurance Risk & Quality Leader

Appendix

Response to the Request for Comments questions: ED 03/18

1. **Have applicable laws and regulations been appropriately addressed in the proposed standard? Are there any references to relevant laws or regulations that have been omitted?**

Yes, we believe the proposed standard takes into account the applicable laws and regulations. We are not aware of any references to relevant laws or regulations that have been omitted.

2. **Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

None noted.

3. **Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?**

None noted.

4. **What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of the proposed standard? If significant costs are expected, the AUASB would like to understand:**

- a) **Where those costs are likely to occur;**
- b) **The estimated extent of the costs, in percentage terms (relative to audit fee); and**
- c) **Whether expected costs outweigh the benefits to the users of audit services?**

The expectation is that due to the substantial revision of the standard there will be additional costs. It is difficult to assess the extent of the costs at this stage, but these will

include initial implementation costs as well as potentially increased audit effort on some audits.

- 5. What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ISA 540 (specific questions/examples would be helpful)?**

We believe that additional guidance on the expected information and documentation under the new standard for those responsible for the accounting estimate and disclosures would be beneficial.

- 6. Over the course of the development of the IAASB's ISA 540, the AUASB discussed a number of issues that were raised by Australian stakeholders at various feedback sessions. The AUASB provided feedback on these matters directly to the IAASB. The IAASB has sought to address these issues in the development of the final ISA 540 that the AUASB now exposes as ED 03/18. Accordingly, the AUASB now seeks specific stakeholder feedback on the following requirements and related application material to the proposed standard:**

a) Paragraph 27: *Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty*

b) Paragraph 30: *Other Considerations Relating to Audit Evidence*

c) Paragraph 33: *Overall Evaluation Based on Audit Procedures Performed*

We believe that the matters raised by the AUASB have been addressed in the standard and support that the standard requires the appropriate application of professional scepticism.

- 7. Are there any other significant public interest matters that constituents wish to raise?**

None noted

The Chair
Auditing and Assurance Standards Board
PO Box 204, Collins Street West
Melbourne Victoria 8007
Australia

15 October 2018

Dear Roger,

Exposure Draft ED 03-18 proposed re-issuance of Auditing Standard ASA 540 Auditing Accounting Estimates and Related Disclosures and & ED 04-18 proposed Auditing Standard ASA 2018-2 Amendments to Australian Auditing Standards

Ernst & Young Australia welcomes the opportunity to offer its views on the exposure draft, Proposed Auditing Standard ASA 540 (Revised) Auditing Accounting Estimates and Related Disclosures (ED 03/18) and Proposed Auditing Standard ASA 2018-2 Amendments to Australian Auditing Standards (ED 04/18), issued by the Auditing and Assurance Standards Board (AUASB).

Overall, we support the proposed amendments outlined in ED-03/18 and ED-04/18 which arise from changes made by the International Auditing and Assurance Board to ISA 540 (Revised) Auditing Accounting Estimates and Related Disclosures. These changes are aimed at enhancing the current ASA 540 to reflect the evolving nature of financial reporting standards that address accounting estimates, as well as the auditing challenges that arise therefrom. We believe that the auditing and assurance standards in Australia should be closely aligned to and consistent as possible with its international equivalents.

Our views on the AUASB's specific questions in relation to ED-03/18

1. Have applicable laws and regulations been appropriately addressed in the proposed standard?
2. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?
3. Are there any principles and practices considered appropriate in maintaining or improving audit quality in Australia that may, or does, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

We believe that all applicable laws and regulations have been appropriately addressed in the proposed ED-03/18. We are not aware of any omitted references. Furthermore, we are not aware of any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard.

4. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of audit services?
5. What, if any, implementation guidance auditors, preparers and other stakeholders would like the AUASB to issue in conjunction with the release of ASA 540 (specific questions / examples would be helpful)
6. The requirements and related application material to the proposed standard: (a) Paragraph 27: Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty; Paragraph 30: Other Considerations Relating to Audit Evidence; and (c) Paragraph 33: Overall Evaluation Based on Audit Procedures Performed

With regard to paragraph 27 and related application guidance on Management's Selection of a Point Estimate and Related Disclosures about Estimation Uncertainty

- The Director's responsibility in relation to the preparation and fair presentation of the financial report include the responsibilities to address estimation uncertainties by selecting an appropriate point estimates and by developing related disclosures about estimation uncertainties. We are supportive of distinguishing this responsibility in ED-03/18 in the definition of the Auditor's point estimate or auditor's range as one developed in evaluating management's point estimate and requirement in paragraph 27(a) to request management to perform additional procedures.

With regard to the enhancements to the auditor's work effort for disclosures related to accounting estimates, we have the following specific concerns:

- We are concerned about changing the criterion for the auditor's evaluation of disclosures related to accounting estimates to "reasonable" from "adequate". Although we conceptually agree with the explanation provided in paragraph 9, we believe such a definition leads to the need for the AUASB to further consider whether the term "reasonable" should be replaced with the clearer terminology in the context of disclosures about the accounting estimates.
- Implications for the auditor's evaluation of misstatements in disclosures - Paragraphs A17 of ASA 450¹, and A3 and A7 of ASA 705 (Revised)² guide the auditor in evaluating whether misstatements in disclosures are material. This guidance, referenced in ED-03/18 in paragraph A142, speaks to the appropriateness, accuracy and adequacy of disclosures, and it is unclear how the AUASB's proposed change in ED-03/18 to evaluate their "reasonableness" affects the auditor's evaluation of material misstatements in accordance with ASA 450. This disparity in terminology runs the risk of the auditor making inappropriate judgments about whether the financial statements are materially misstated. As expressed, we believe the terminology for evaluation of disclosures, if changes are pursued in conjunction with ED-03/18, needs to be aligned across the ASAs, in particular across ED-03/18, ASA 450, ASA 700 (Revised) and ASA 705 (Revised)³. Accordingly, additional guidance is required to support the conforming amendment proposed to paragraph 13 (c) to read "the accounting estimates and related disclosures are reasonable".

With regard to Overall evaluation based on audit procedures performed, our significant views and areas of concern are:

- We support the consideration of all relevant audit evidence, whether corroborative or contradictory, as required in paragraph 34 of ED-03/18. However, we believe the last sentence of paragraph 34 appears to be misplaced because it addresses the implications of the auditor not obtaining sufficient appropriate audit evidence. These implications seem to be more closely related to evaluations performed in paragraph 33(a) and 33(b) of ED-03/18.
- We do not believe the determination of whether disclosures beyond those required by the financial reporting framework, which is currently included in paragraph 36 of ED-03/18, should be included in the requirements. Including this evaluation in the requirements, in our view, de-emphasizes the importance of the auditor's evaluation of whether the disclosures are in accordance with the requirements of the financial reporting framework, which we believe is challenging in itself.

Because paragraphs 13 and 14 of ASA 700 (Revised) address the auditor's evaluation of fair presentation of the financial statements, including the disclosures, we believe it would be more appropriate for the application material in ED-03/18 to address and explain the relationship of the

¹ ASA 450, Evaluation of Misstatements Identified during the Audit

² ASA 705 (Revised), Modifications to the Opinion in the Independent Auditor's Report

³ ASA 700 (Revised), Forming an Opinion and Reporting on Financial Statements

required overall evaluation of estimates and related disclosures to the evaluation of fair presentation in ASA 700 (Revised). In this regard, we believe such application material would be best placed in support of the overall evaluation in paragraph 35 of ED-03/18.

7. Are there any other significant public interest matters that constituents wish to raise?

In our view there are no other significant public interest matters to raise.

We welcome the opportunity to contribute to the improvement of Auditing and Assurance Standards that will continue to drive the quality and consistency of such services in Australia. We would be pleased to discuss our comments with members of the Auditing and Assurance Standards Board and its staff. Should you wish to do so, please contact Kathy Parsons (Kathy.Parsons@au.ey.com or on (02) 8295 6882).

Yours sincerely



Kathy Parsons
Partner



August 2014

**PRINCIPLES OF CONVERGENCE TO
INTERNATIONAL STANDARDS OF THE
INTERNATIONAL AUDITING AND ASSURANCE
STANDARDS BOARD (IAASB)**

AND

**HARMONISATION WITH THE STANDARDS OF THE
NEW ZEALAND AUDITING AND ASSURANCE
STANDARDS BOARD (NZAuASB)**

Obtaining a Copy of this Document

This publication is available on the AUASB website: www.auasb.gov.au

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Principles of Convergence to International Standards of the International Auditing and Assurance Standards Board (IAASB)

and

Harmonisation with the Standards of the New Zealand Auditing and Assurance Standards Board (NZAuASB)

Application Date

1. The policies detailed in this paper apply from 1 August 2014.

Introduction

2. The key strategic objectives set by the Financial Reporting Council (FRC) for the Auditing and Assurance Standards Board (AUASB) include using the International Standards on Auditing (ISAs) to develop Australian Auditing Standards, and modifying the ISAs to conform to the Australian regulatory environment.

Objectives

3. In implementing the FRC's strategic direction, the AUASB has determined the following objectives:
 - (a) To adopt international auditing and assurance standards in Australia unless there are strong reasons not to (which the AUASB describes as "compelling reasons"); and
 - (b) To work with the New Zealand Auditing and Assurance Standards Board (NZAuASB) towards the establishment of harmonised standards based on international standards.

Policies

4. The AUASB may consider modifying international standards for application in Australia under either of those objectives. The AUASB considers such modifications acceptable provided that they consider the public interest¹, and do not conflict with, or result in lesser requirements than, the international standards.
5. The purpose of this paper is to set out the principles of convergence to international standards and harmonisation with New Zealand standards to be used as the framework for the standard setting process of the AUASB.
6. It is expected that this paper will be revised from time to time to take account of changes to the Australian financial reporting framework.
7. The principles of convergence set out in this paper adhere to the principles set out in the IAASB Policy Position, *Modifications to International Standards of the IAASB - A Guide for National Standard Setters that Adopt IAASB's International Standards but Find it Necessary to Make Limited Modifications* (July 2006).
8. The principles of convergence to the IAASB standards are set out in a flowchart in Appendix 1, and the principles of harmonisation with the New Zealand standards are set out in a flowchart in Appendix 2.

¹ IFAC defines the public interest as "*The net benefits derived for, and procedural rigor employed on behalf of, all society in relation to any action, decision or policy*". Refer IFAC Policy Position 5, *A Definition of the Public Interest*, June 2012.

Overarching principles of convergence with International Standards

9. The international standards should be adopted, and should be modified only if there are compelling reasons to do so.
10. In the case of an international standard that is being reviewed for the purpose of adoption in Australia, the compelling reasons test for modifications in the public interest is triggered where the international standard does not reflect, or is not consistent with:
 - (a) The Australian regulatory arrangements; or
 - (b) Principles and practices that are considered appropriate in Australia (including in the use of significant terminology).
11. Where the international standard does not reflect, or is not consistent with, the Australian regulatory arrangements, the following criteria have to be met before the standard is modified:
 - (a) The standard can be modified so as to result in a standard the application of which results in effective and efficient compliance with the legal framework in Australia; and
 - (b) The modification to the standard does not result in a standard that conflicts with, or results in lesser requirements than, the international standard.
12. Where the international standard does not reflect, or is not consistent with, principles and practices that are considered appropriate in Australia, the following criteria have to be met before the standard is modified:
 - (a) The standard can be modified so as to result in a standard that:
 - (i) The application of which results in compliance with principles and practices considered appropriate by the AUASB;
 - (ii) Is clear and promotes consistent application by all practitioners in Australia;
 - (iii) Promotes significant improvement in audit/assurance quality (as described by the IAASB's *Framework for Audit Quality*) in the Australian environment; and
 - (b) The relative benefits of modifying the standard outweigh the costs (with cost primarily being compliance cost and the cost of differing from international standards and the New Zealand standards, and benefit primarily relating to audit/assurance quality); and
 - (c) The modification to the standard does not result in a standard that:
 - (i) Conflicts with, or results in lesser requirements than, the international standard;
 - (ii) Is overly complex and confusing; or
 - (iii) Inadvertently changes the meaning or intent of the international standard wording or places more onerous requirements on practitioners in Australia than necessary.

Overarching principles of harmonisation with New Zealand Standards

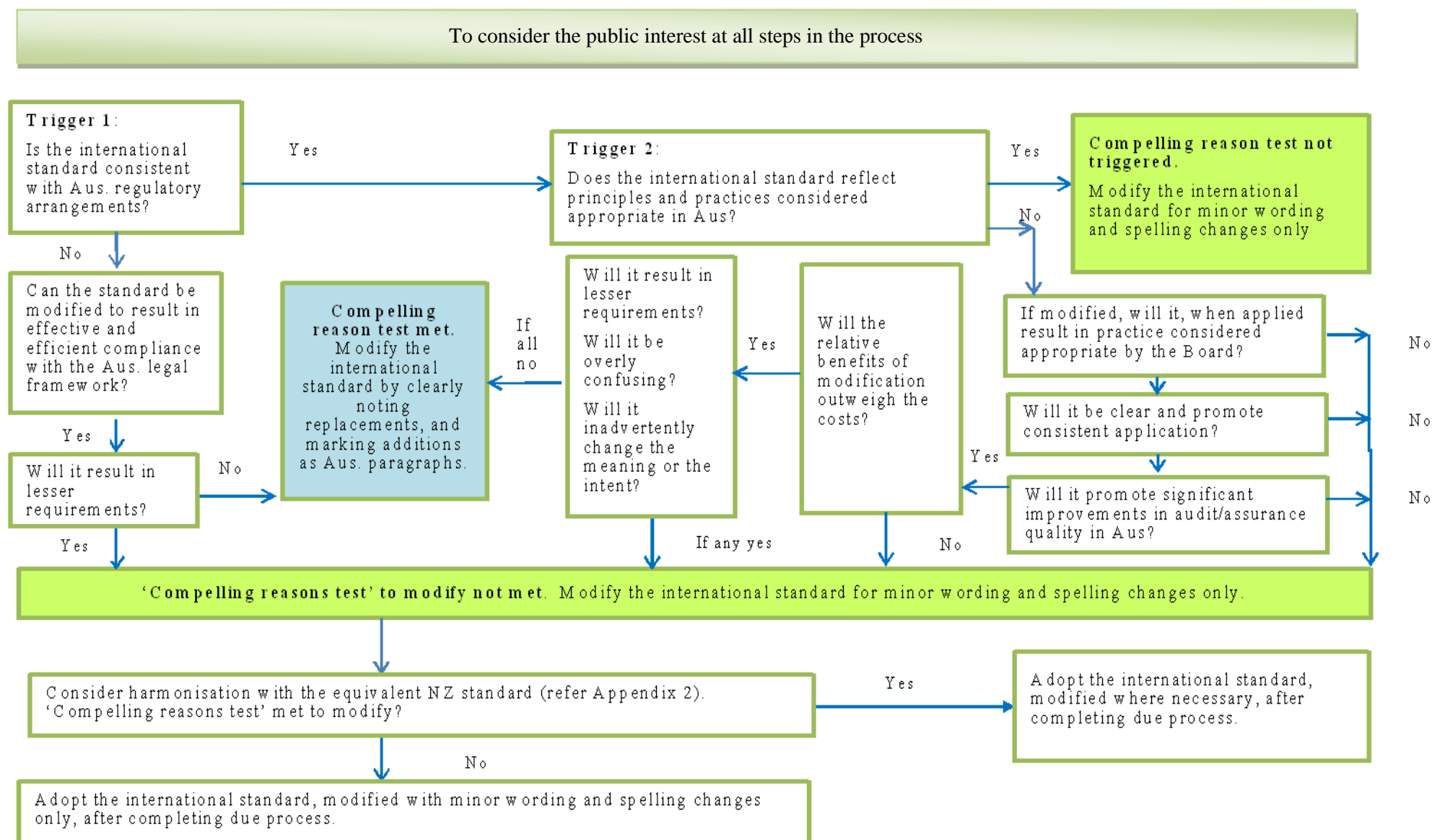
13. When considering harmonisation with a New Zealand standard, the compelling reasons test for modification of the international standard in the public interest is triggered where the New Zealand standard covers a matter not covered in the international standard, and that gap is also relevant in the Australian standard.
14. Once the compelling reason test has been triggered, the following criteria have to be met before the standard is modified:
 - (a) The standard can be modified so as to result in a standard that:

- (i) The application of which results in compliance with the legal framework or principles or practices considered appropriate by the AUASB;
 - (ii) Is clear and promotes consistent application by all practitioners in Australia;
 - (iii) Promotes significant improvements in audit/assurance quality (as described by the IAASB's *Framework for Audit Quality*) in the Australian environment; and
- (b) The relative benefits of modifying the standard outweigh the costs (with cost primarily being compliance cost and cost of differing from the international standard and the benefit primarily relating to audit/assurance quality); and
- (c) The modification to the standard does not result in a standard that:
 - (i) Conflicts with, or results in lesser requirements than, the international standard;
 - (ii) Is overly complex and confusing; or
 - (iii) Inadvertently changes the meaning or intent of the international standard wording or places more onerous requirements on practitioners in Australia than necessary.

General

15. When considering developing a standard for which there is no equivalent international standard, compelling reasons for developing the standard are:
 - (a) The standard addresses public interest matters within the Australian environment;
 - (b) The standard will promote significant improvements in audit/assurance quality in the Australian environment; and
 - (c) The benefits of applying the standard will outweigh the costs (with costs primarily being compliance costs and benefits primarily relating to audit/assurance quality).
16. The development of an Australian standard should be harmonised with the equivalent New Zealand standard by adopting the New Zealand standard, where applicable. Compelling reasons for differences between Australian and New Zealand standards are where:
 - (a) Different regulatory requirements apply; and/or
 - (b) Different practices are considered appropriate (including the use of significant terminology).
17. Any deletions from the international standards should be clearly noted, and any additions clearly marked as Australian paragraphs.
18. Minor wording and spelling changes (as opposed to changes reflecting the use of significant terminology), where the intent remains the same, need not be reflected in the Australian standard as a modification to the international standard.
19. Each AUASB Standard issued prior to 1 July 2012 will be assessed for compliance with the policies in this paper in accordance with the AUASB work program.

Flowchart to Depict the ‘Compelling Reasons Test’ in the Principles of Convergence with the IAASB Standards



Flowchart to Depict the 'Compelling Reasons Test' in the Principles of Harmonisation with the New Zealand Standards

