

Board Meeting Agenda

5 September 2018

9.15 am to 5.00pm

The Heritage Hotel, 35 Hobson Street, Calder Mackay 1, Auckland

Est. Time	Item	Topic	Objective		Page
A: NON-PUBLIC SESSION					
10.30am	Morning tea				
B: PUBLIC SESSION					
10.45 am	3	<u>Approve Strategic Action Plan 2018/2023</u>			
	3.1	Board meeting summary paper	Note	Paper	
	3.2	Draft NZAuASB SAP 2018/23	Approve	Paper	
	3.3	NZAuASB 2018-21 SAP - Resourcing	Approve	Paper	
	3.4	NZAuASB 2018-21 SAP - Timing	Approve	Paper	
	3.5	Draft NZAuASB SAP 2018/19 Implementation plan	Approve	Paper	
	3.6	XRB Organisation SAP 2017/18 Dashboard	Note	Paper	
11:45 am	4	<u>Meet with practitioners on audit issues</u>			
	4.1	Discussion on current issues	Discuss	Verbal	-
12:45 pm	Lunch				
1.30 pm	5	<u>IAASB ED on ISA 315 (Revised)</u>			
	5.1	Board meeting summary paper	Note	Paper	
	5.2	Issues paper	Consider	Paper	
	5.3	IAASB ED ISA 315 (Revised)	Consider	Paper	Separate
2.15 pm	6	<u>ISA 540</u>			
	6.1	Board meeting summary paper	Note	Paper	
	6.2	Draft Basis of Conclusions (Non-public document)	Note	Paper	
	6.3	ISA 540 (Revised)	Consider	Paper	
	6.4	Conforming and consequential Amendments	Consider	Paper	
3:00 pm	Afternoon tea				
3:15 pm	7	<u>Small NFPs engagements project</u>			
	7.1	Board meeting summary paper	Note	Paper	
	7.2	Issues and project plan	Approve	Paper	
4:00 pm	8	<u>Examination of prospective Information standard</u>			
	8.1	Board meeting summary paper	Note	Paper	
	8.2	Update on project plan	Consider	Paper	
4.15 pm	9	<u>NZ SRE 2410</u>			
	9.1	Board meeting summary paper	Note	Paper	
	9.2	Issues paper	Consider	Paper	
4:35 pm	10	<u>Environmental Scanning</u>			

Est. Time	Item	Topic	Objective		Page
	10.1	International monitoring update	Note	Paper	
	10.2	Domestic monitoring update	Note	Paper	
	10.3	Academic research update	Note	Paper	
C: NON-PUBLIC SESSION					

Next meeting: 24 October 2018, Wellington

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 3.1

Meeting date: 5 September 2018

Subject: NZAuASB Strategic Action Plan

Date: 16 August 2018

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Action Required

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For Information Purposes Only

Agenda Item Objectives

To APPROVE:

- the NZAuASB Strategic Action Plan document for the five-year period 1 July 2018 to 30 June 2023;
- the updated indicative timing schedules for the NZAuASB Strategic Actions for the 2018 to 2023 period; and
- the “annual cut” of the NZAuASB Strategic Action Implementation Plan for 2018/19 identifying the specific actions that will be undertaken in this year.

Background

NZAuASB Strategic Action Plan (SAP)

1. At its July meeting the NZAuASB considered and provided feedback to the CE on the revised XRB organisation Strategic Plan 2018-2023.
2. The Board also considered and provided feedback on a document that showed the NZAuASB Strategic Action Plan, noting for which actions no change are required, and indicating the proposed new actions that reflect the proposed changes based on the discussions at the joint Board Strategy day that were of specific relevance to the NZAuASB, and that accounted for any relevant changes made to the XRB overarching strategic action plan.
3. We have now updated the NZAuASB Strategic Action Plan document for the five-year period 1 July 2018 to 30 June 2023 for approval. A marked-up copy is available at agenda item 3.2. Please note that the format of the document has been changed to align closer with the format of the XRB SAP 2018-2023 document and the NZASB SAP 2018-2023 document. The mark up does not show the format changes.

4. The NZAuASB's planned strategic actions are summarised in the table below. The proposed changes are highlighted.
5. The only areas identified at the July meeting where changes to the NZAuASB's actions are required are under Specific Strategy 1, Part B: *Address Critical Issues* and Strategy 4: *Enhance Constituency Engagement*. The main changes are:
 - Deleting previous Action 1B.4: Adopting the revised AUP International Standard. This is because of the delay in obtaining the mandate to issue an AUP standard, and to leave it as business as usual once the mandate is obtained.
 - Adding new Action 1 B.7: Perform a post implementation review on the Compliance Engagement Standard, to replace previous action 1B.8 Developing guidance on the use of the Compliance Engagement Standard.
 - Adding new Action 1 B.9: Review the compelling reason test.
 - Deleting previous action 1B.10: Consider developing guidance for Audit Committees and adding new Action 4.10 Facilitating the Enhancement of Audit quality, to capture the action to consider approaching other relevant participants in the reporting chain (for example MBIE, IoD, NZX, FMA and the audit firms) to determine if there is an appetite for the joint development of a best practice guide for audit committees in New Zealand.
 - Deleting Actions 2.1 and 2.2 as the research projects have been completed.
 - Deleting previous Action 4.8: Promoting understanding of the new NOCLAR requirements.
6. Subsequent to the July meeting we have identified the following actions that we recommend also be included in the SAP:
 - Adding new action 2.1 Undertake user needs research as appropriate. There are no current areas of research the NZAuASB has identified, but it remains part of the strategic action plan of the Board and the XRB. The action will comprise:
 - Identifying and performing applicable user needs research to undertake where appropriate.
 - Using the research outcomes of the XRB Organisation as a basis for considering future enhancements to the auditing and assurance standards and to help inform efforts to influence the work of the international standard setting boards.
 - Adding new Action 4.8: Promoting understanding of the new Restructured Code of Ethics.
7. The proposed changes are summarised in the table below.

Strategic Plan Strategy	Action
Specific Strategy 1: Maintain & Enhance Existing Standards – Part A: Maintain Existing Suites of Standards (Business as Usual)	Action 1A.1: Contributing to International Due Process
	Action 1A.2: Maintaining New Zealand Standards
	Action 1A.3: Monitoring the Assurance

	Environment
Specific Strategy 1: Maintain & Enhance Existing Standards – Part B: Address Critical Issues	Action 1B.1: Developing Guidance on Assurance on Non-Financial Information
	Action 1B.2: Developing an Assurance Standard on the Examination of Prospective Information
	Action 1B.3: Developing an Auditing Standard on Auditing of Service Performance Information
	Action 1B.4: Adopting the revised IAASB Standard on Agreed Upon Procedures
	Action 1B.5 4: <u>Consider what further Developing Guidance is needed on the use of the XRB auditing and assurance standards and relevant assurance products and develop guidance where identified.</u>
	Action 1B.65: Developing a Review Standard on Reviewing of Service Performance Information
	Action 1B.76: Developing an Engagement Standard/Guidance for smaller NFPs to better meet the needs of users, as informed by research completed in 2016-2017.
	<u>Action 1B.8: Develop Guidance on the use of the Compliance Engagement Standard</u>
	<u>Action 1B.7 Perform a post implementation review on the use of the Compliance Engagement Standard</u>
	Action 1B.98: Developing guidance or amending NZ SRE 2410 <i>Review of Financial Statements Performed by the Independent Auditor of the Entity</i>
	<u>Action 1B.10: Consider developing guidance for Audit Committees, similar to the audit committee practice guide recently issued in Australia.</u>
Specific Strategy 2: Undertake User-Needs Research	<u>Action 2.1: Researching Assurance Needs of Users of Non-Public Interest Entities Reports</u>
	<u>Action 2.1 Undertake user needs research as appropriate</u>
	<u>Action 2.2: Obtaining a better understanding about the integrity of the application of the International Standard of Assurance Engagements (New Zealand) 3000 (Revised); Assurance Engagements Other than Audits or Reviews of Historical Financial Information.</u>
Specific Strategy 3: Influence the	Action 3.1: Building Relationships with the

International Boards	IAASB
	Action 3.2: Increasing the International Visibility of the NZAuASB
	Action 3.3: Building Relationships with the IESBA
Specific Strategy 4: Enhance Constituency Engagement and Support	Action 4.1: Enhancing Due Process Consultation
	Action 4.2: Undertaking On-Going Dialogue
	Action 4.3: Improving Engagement Relating to Other Assurance Reports
	Action 4.4: Improving Engagement with Small Assurance Practitioners
Specific Strategy 4: Enhance Constituency Engagement and Support <i>continued</i>	Action 4.5: Promoting Understanding of Other Assurance Engagements
	Action 4.6: Promoting Greater Understanding of the Purpose of Audits and Reviews
	Action 4.7: Promoting Understanding of the New Auditor Reporting Requirements
	Action 4.8: Promoting Understanding of the New NOCLAR Reporting Requirements
	Action 4.8: Promoting understanding of the new restructured Code of Ethics
	Action 4.9: Promoting Understanding of the Factors that Affect Audit Quality
	Action 4.10: Facilitating the Enhancement of Audit Quality

8. We have also updated the indicative timing and indicative resource schedules that the Board approved in 2017. Agenda Paper 3.3 provides the suggested broad timing for the NZAuASB's strategic actions, together with an indication of the broad magnitude of the likely resourcing required for each strategic action. We believe that we have adequate resources to implement the strategic actions.
9. Agenda paper 3.4 provides the suggested, more specific, timing for the NZAuASB's strategic actions. The suggested timing has been updated to cover the next three years of the strategic period, with the remaining two years deliberately not covered in detail at this point given how far away they are.
10. The main changes to the timing schedule at agenda item 3.4 are our recommendation to:

- Extend the completion date of Action 1B.2 Developing an assurance standard on Prospective Information by 6 months to Dec 2019. We started this project in 2017/18 but it has been delayed due to other competing priorities.
 - Extend the completion date of Action 1B.5 Developing a review standard on Service Performance Information by 16 months to June 2020. The start of this project has been delayed until after the auditing standard has been issued.
 - Extend the completion date of Action 1B.6 Developing an Engagement standard/guidance for smaller NFPs by 6 months to Dec 2019. This project has been delayed due to other competing priorities.
 - Carry forward Action 1B.8 Developing guidance or amending NZ SRE 2410 that was planned for completion in 2017/18 to be completed in 2018/19. This project has been delayed due to other competing priorities.
11. The “annual cut” of the NZAuASB Strategic Action Implementation Plan for 2018/19, identifying the specific actions that will be undertaken in this year is available at agenda 3.5, and is based on the timing identified in agenda 3.4. The proposed changes have been marked up.
12. We have also included, for noting only, the XRB Organisation SAP 2017/2018 dashboard to June 2018 that was presented to the XRB Board at its August meeting.

Matters to consider

13. We specifically request feedback from the Board on whether the Board agrees with:
- the new actions 4.8 and 2.1 added in the development of the SAP 2018-2023;
 - the allocated timing and prioritising of the various actions in the SAP; and
 - the planned actions noted against each strategic action in the Strategic Action Implementation Plan for 2018/19.

Recommendation

We recommend that the Board APPROVE, subject to feedback received at the meeting:

- the NZAuASB Strategic Action Plan document for the five-year period 1 July 2018 to 30 June 2023;
- the updated indicative resourcing and indicative timing schedules for the NZAuASB Strategic Actions for the 2018 to 2021 period; and
- the “annual cut” of the NZAuASB Strategic Action Implementation Plan for 2018/19, identifying the specific actions that will be undertaken in this year.

Material Presented

Agenda item 3.1	Board Meeting Summary Paper
Agenda item 3.2	NZAuASB SAP 2018-2023
Agenda item 3.3	NZAuASB 2018-21 Strategic Action Plan- Indicative Resourcing
Agenda item 3.4	NZAuASB 2018-21 Strategic Action Plan- Indicative Timing
Agenda item 3.5	NZAuASB Strategic Action Implementation Plan for 2018/19
Agenda item 3.6	XRB Organisation SAP 2017/2018 dashboard to June 2018

*~~"Giving Life to the A User-
Needs Framework for New
Zealand's Wellbeing"~~*

Strategic Action Plan

**For the five year period
1 July 2018 to 30 June 2023**

September 2018

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1. Overview of the NZAuASB

The New Zealand Auditing and Assurance Standards Board (NZAuASB) is a Committee of the External Reporting Board (XRB) established under schedule 5 of the Crown Entities Act.

The NZAuASB has delegated authority from the XRB Board to develop or adopt and issue auditing and assurance standards (including professional and ethical standards for assurance practitioners). In doing so the NZAuASB must operate with the financial reporting strategy established by the XRB Board.

The NZAuASB also issues "Other Assurance Standards" in accordance with an [authority provided](#) by the Minister of Commerce issued under section 24 (1) (b) (v) of the Financial Reporting Act 1993.

1.1 NZAuASB Outcome Goal

The NZAuASB's strategic objective is:

To establish auditing and assurance standards which will encourage assurance providers to behave and provide assurance in a manner that engenders confidence in New Zealand financial reporting, assists entities to compete internationally, and enhances entities' accountability to stakeholders.

The provision of high quality assurance that provides users with confidence about the fair presentation of the information presented in financial reports is vital to the achievement of the XRB's outcome goal. The NZAuASB considers the suite of auditing and assurance standards, and how they are being applied, with this objective in mind. The NZAuASB issues such standards or guidance as it considers necessary from time to time to achieve its strategic objective.

1.2 Role and Responsibilities of the NZAuASB

The primary responsibility of the NZAuASB is to develop or adopt, expose, finalise and promulgate:

- auditing and assurance standards for use in audit or assurance engagements required by statute;
- professional and ethical standards to be applied by assurance practitioners undertaking statutory assurance engagements; and
- other assurance standards within the scope of any "additional assurance standards" approval provided by the Responsible Minister in accordance with the Financial Reporting Act 2013.

Other more specific responsibilities include:

- ensuring that the auditing and assurance standards are consistent with the "financial reporting strategy" established from time-to-time by the XRB Board, including:
 - adoption of international standards;

- development of standards jointly with Australia; or
 - development of New Zealand specific standards as may be required by the strategy;
- developing and promulgating guidance material to support the application of issued standards as necessary;
- undertaking or commissioning research relating to auditing and assurance or matters concerning professional and ethical conduct;
- working with the Australian Auditing and Assurance Standards Board (AUASB), through reciprocal membership and liaison, and occasional joint meetings, to promote cooperation and the harmonisation of New Zealand and Australian auditing and assurance standards within the parameters of the financial reporting strategy established by the XRB Board;
- working with the Accounting Professional and Ethical Standards Board of Australia (APESB), through liaison and observing APESB meetings, to promote cooperation and harmonisation of New Zealand and Australian professional and ethical standards for assurance practitioners;
- preparing submissions to international standard setting bodies responsible for auditing and assurance and professional and ethical standards on exposure drafts issued by them and/or matters of importance to auditing and assurance in New Zealand;
- liaising with, and contributing to the work of, international standard setting bodies in areas of importance to auditing and assurance in New Zealand and which are consistent with the XRB Board's financial reporting strategy;
- participating in relevant international fora and groupings, including those involving national standard-setters;
- contributing as appropriate to the development and implementation of the XRB's Strategic Plan; and
- act as thought leaders on assurance issues.

The NZAuASB's Strategic Action Plan reflects these responsibilities.

2. Introduction to the NZAuASB's Strategic Action Plan

2.1 The NZAuASB's Strategic Action Plan

This document is the Strategic Action Plan of the NZAuASB. It outlines the specific actions that the NZAuASB intends to take in the 2018/19 financial year and subsequent years to give effect to the XRB's overarching strategic plan. Those actions are consistent with the roles and responsibilities of the NZAuASB as outlined in section 1.2.

It is intended to update and revise this NZAuASB Strategic Action Plan annually during the five year period covered by the overarching strategic plan. This will help ensure that

the Strategic Action Plan is a dynamic document that reflects achievements to date and new subsequent actions.

The NZAuASB's output priorities and delivery mechanisms are aligned with the XRB's Strategic Plan for the period 2018-2023. A summary of the XRB's Strategic Priorities for the 2018-2023 period is available in Appendix A.

3. Strategic Priorities for the 2018-2023 period

Key focus areas for A User-needs Framework for New Zealand's Wellbeing

Internationally standard setting structures for auditing & assurance standard setting (including those for ethics) are under review, which may result in some fundamental changes. These are in addition to other disruptions like developments in artificial intelligence, other technology advances and the professional accounting market place. In the period from 1 July 2018 to 30 June 2023 the NZAuASB plans to actively monitor such disruptions and consider the implications for the New Zealand auditing and assurance standards. The NZAuASB further plans to enhance its regional relationships to strengthen its international influence and as a contingency plan in the event of returning to national standard setting.

Also, the XRB plans to take an active role in leading the development of extended external reporting (EER) in New Zealand as it relates to users of "corporate" reports. The NZAuASB will monitor the XRB EER project, contributing to the development of guidance as appropriate, and considering the implications for New Zealand auditing and assurance standards.

The NZAuASB's outcome goal in the period 2018-2023 will be achieved through several specific strategies, as set out below, split between an Overarching Strategy, Business as Usual Activities and Specific Strategic Actions.

Overarching Strategy – Broad strategic approach
<ul style="list-style-type: none"> • Maintaining and enhancing the existing suite of auditing and assurance standards (including professional and ethical standards for assurance practitioners); • Continuing the convergence and harmonisation approach (where relevant) for auditing and assurance standards; • Working to ensure that New Zealand's auditing and assurance standards are understood and applied in accordance with the NZAuASB's strategic objective; and • <u>Responding to the rapidly changing international environment and external reporting landscape</u>
Business as Usual Activities
<p>This section outlines the "business as usual" activities that the NZAuASB will undertake during the strategic period. These activities comprise the actions required to maintain the existing suites of standards in accordance with the overarching strategy (convergence with international standards, and harmonisation with Australian standards where appropriate). To a large</p>

extent these activities are a continuation of the activities undertaken by the NZAuASB during the previous strategic period.

Specific Strategy 1: Part A : Maintain Existing Suite of Standards

The purpose of this strategy is to ensure that the existing suites of standards are maintained on an on-going basis so that they are fully converged with international standards and harmonised with Australian standards where appropriate at all times.

The actions required under this strategy are those necessary to ensure convergence and harmonisation is maintained, including actively monitoring any issues emerging from the implementation of standards, and responding to those issues where appropriate.

Specific action	This action will comprise...
Action 1A.1: Contributing to International Due Process	<p>Actively contributing to the “due process” activities of the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA), by:</p> <ul style="list-style-type: none"> a. Ensuring assurance practitioners and relevant users of assurance reports are aware of the IAASB and the IESBA due process documents and encouraging them to make submissions directly to the international boards and to the NZAuASB; b. Responding, as appropriate, to the IAASB and the IESBA due process documents (consultation documents, discussion papers and exposure drafts) and doing so in conjunction with the AUASB and the Australian Professional Ethical Standards Board (APESB) where appropriate; c. Participating, as appropriate, in roundtables and other face-to-face due process related meetings organised by the international boards.
Action 1A.2: Maintaining New Zealand Standards	<p>Amending the auditing and assurance standards (auditing standards, review engagement standards, other assurance standards) to ensure that the existing suites of standards are maintained on an on-going basis, by:</p> <ul style="list-style-type: none"> a. Incorporating any auditing and assurance standards, or amendments to those standards, issued by the IAASB, to achieve convergence, and including working with the AUASB to ensure any changes are appropriately harmonised. b. Incorporating any professional and ethical standards, or amendments to those standards, issued by the IESBA, including liaising with the APESB to ensure any changes are appropriately harmonised. c. Responding as appropriate to any gaps /issues identified with the current suite of standards identified. d. Incorporating any amendments to international standards to domestic standards where applicable, including in collaboration with the AUASB.

Action 1A.3: Monitoring the Assurance Environment	<p>Monitoring the wider assurance environment and considering the implications of any developing issues for New Zealand auditing and assurance standards.</p> <ol style="list-style-type: none"> Monitoring issues arising from the implementation of the current suite of standards and responding as appropriate; Monitoring issues or gaps with the current suite of standards and responding as appropriate. Tracking local and international research projects and considering the implications for the New Zealand auditing and assurance standards; Monitoring results from QA reviews conducted locally and internationally and considering the implications for New Zealand auditing and assurance standards; Contributing to government policy work relating to auditing and assurance standards; Building relationships and liaising with other relevant NSSs on matters of mutual interests (<u>specifically on the use of data analytics and audit of SMEs</u>); <u>Monitoring the assurance environment for changes coming out of the Monitoring Group</u> <u>Keeping a watching brief over the possible restructuring of firms and the impact on the assurance environment.</u> <u>Monitoring the XRB EER project, contributing to the development of reporting guidance as appropriate, and considering the implications for New Zealand auditing and assurance standards.</u> <u>Monitoring activities and developments in the wider assurance standard setting space and considering the implications for the New Zealand auditing and assurance standards</u>
<p><u>Specific Strategic Actions</u></p> <p>This section outlines the new specific strategic actions that the NZAuASB intends to carry out during the period of the strategic plan. These strategic actions comprise activities that would not normally be undertaken as part of the business as usual actions outlined in section 3.</p> <p>They also relate to issues or matters not addressed (or addressed in any detail) by the NZAuASB previously.</p>	
<p>Specific Strategy 1: Part B : Address critical issues</p> <p>The purpose of this strategy is to address any deficiencies or gaps in existing standards that are critical to user-needs and the quality of financial reporting. The actions required under this strategy are to (a) identify critical issues; and (b) undertake appropriate actions to address those critical issues within a reasonable timeframe.</p>	

The NZAuASB's primary focus is on promulgating auditing and assurance standards. The Board spent the 2009-2014 period developing and issuing amended standards to give effect to the new Auditing & Assurance Standards Framework. Many of these new standards became effective during the 2014-2016 period and critical issues may emerge that need to be addressed. The Board will do so should this occur.

In addition, the NZAuASB is aware of a small number of critical issues with the existing standards that it plans to address during the 2018-2023 period:

Specific action	This action will comprise...
Action 1B.1: Developing Guidance on Assurance on Non-Financial Information other than service performance information	<ul style="list-style-type: none"> a. Obtaining a greater understanding of the assurance engagements on non-financial information being carried out in New Zealand. b. Developing the guidance in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.
Action 1B.2: Developing an Assurance Standard on the Examination of Prospective Information	Developing the standard in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.
Action 1 B3: Developing an Auditing Standard on Auditing Service Performance Information	Developing an auditing standard on auditing service performance for Public Benefit Entities (PBEs) ¹ in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.
Action 1 B4: Consider what further guidance is needed on the use of the XRB auditing and assurance standards and relevant assurance products and develop guidance where identified.	<ul style="list-style-type: none"> a. Considering what further guidance is needed that explain the difference between reasonable and limited assurance, as well as various assurance products that are available, relevant standards to use, how to deal with unclear assurance requirements, and the correct terminology to use when setting assurance requirements in legislation and/or policies. b. Developing appropriate guidance.
Action 1 B5: Developing a Review Standard on Reviewing Service Performance Information	Developing a review standard on reviewing service performance for Public Benefit Entities (PBEs) in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.
Action 1 B6: Developing an Engagement Standard/Guidance for smaller NFPs	Developing an engagement standard/guidance for smaller NFPs, not required by statute to have an audit or review, to better meet the needs of users, as informed by research completed in 2016-17, in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.
Action 1 B7: Perform a post implementation	Performing a post implementation review on the Compliance Engagement Standard jointly with the AUASB

¹ This action reflects the new accounting standards that require PBEs to include both financial and non-financial information in their general purpose financial reports to report their performance. In addition many PBEs are required by legislation to report service performance information.

review jointly with the AUASB on the Compliance Engagement Standard	to determine if further guidance is needed.
Action 1 B8: Developing Guidance or amending NZ SRE 2410 Review of Financial Statements Performed by the Independent Auditor of the Entity	<ul style="list-style-type: none"> a. Considering whether to amend the standard or to develop guidance, similar to guidance developed by the AUASB, for the new auditor reporting requirements and NOCLAR. b. Amending the standard in accordance with the due process for domestic standards or developing guidance similar to the AUASB guidance.
<u>Action 1 B9: Review the compelling reason test</u>	<ul style="list-style-type: none"> a. <u>Performing a review of the compelling reason test, in collaboration with the AUASB, to determine if it remains fit for purpose</u> b. <u>Liaising with the AUASB about any changes that may be needed.</u>
Specific Strategy 2: Undertake User-Needs Research <p>A key objective of the XRB is to ensure that auditing and assurance standards are based on a user-needs approach i.e. the assurance reports required by those standards provide the level of assurance and information required by users of those assurance reports for accountability and decision-making purposes. This strategy involves undertaking deliberate, organised research into needs of the various users of NZAuASB standards as a basis for considering enhancements to the NZAuASB's standards in the future, and to help inform efforts to influence the work of the international standard setting boards.</p>	
Specific action	This action will comprise...
<u>Action 2.1 Undertake user needs research as appropriate</u>	<ul style="list-style-type: none"> a. <u>Identifying and performing applicable user needs research to undertake where appropriate.</u> b. <u>Using the research outcomes of the XRB Organisation as a basis for considering future enhancements to the auditing and assurance standards and to help inform efforts to influence the work of the international standard setting boards.</u>
Specific Strategy 3: Influence the International Boards <p>A key aspect of the overarching strategy contained in the XRB Strategic Plan is the international convergence approach. Implicit in this approach is the need for the NZAuASB to mostly be a "standard-taker" i.e. to use the international standards as the base for New Zealand standards. For those standards to be appropriate in New Zealand, it is important for the NZAuASB to seek to influence international standards "at the front end" (i.e. during their development stage) as the ability to influence the content of international standards once an exposure draft is issued is limited.</p> <p>The purpose of Specific Strategy 3 is to seek to influence the work of the international boards during the early stages of standards development through the establishment of "influencing strategies" specific to each international board.</p> <p>The NZAuASB's specific strategic actions relating to Specific Strategy 3 reflects the Board's responsibilities for promulgating auditing and assurance standards. Its influencing strategies are</p>	

therefore targeted at the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA).	
Action 3.1: Building Relationships with the IAASB	<ul style="list-style-type: none"> a. Attending relevant meetings and events (including National Standard Setters (NSSs) meetings); b. Taking opportunities to meet with IAASB members and staff; c. Fostering relationships with Australasian representatives on the IAASB and those who are involved in relevant working groups; d. Hosting IAASB members and staff in visits to New Zealand; e. <u>Collaborating with other NSSs to better influence the IAASB agenda and other global initiatives.</u>
Action 3.2: Increasing the International Visibility of the NZAuASB	<ul style="list-style-type: none"> a. Volunteering to present at the NSS meetings on New Zealand projects or with the AUASB on joint projects; and b. Identifying appropriate, mutually beneficial IAASB projects and contributing technical resources in support of those projects.
Action 3.3: Supporting Lyn Provost in her role as IAASB member	<ul style="list-style-type: none"> a. Inviting Lyn Provost to Board meetings; b. Arranging meetings with the Technical Advisory Group to receive input before each IAASB meeting; and c. The Director Assurance Standards attending IAASB meetings as Technical Advisor (TA) to Lyn Provost.
Action 3.4: Building Relationships with the IESBA	<ul style="list-style-type: none"> a. Attending relevant meetings and events (including NSS meetings); b. Taking opportunities to meet with IESBA members and staff; and c. Fostering relationships with Australian representatives on the IESBA.
Specific Strategy 4: Enhance Constituency Engagement and Support Another key aspect of the NZAuASB's standard setting strategy is to ensure that standards are developed in collaboration with the constituency. This is reflected in Specific Strategy 4 which has three elements: Constituent engagement, awareness raising activities and sector facilitation.	
Specific action	This action will comprise...
<i>Constituent Engagement: establish ways for the NZAuASB to enhance the level and quality of constituent engagement.</i>	

Action 4.1: Enhancing Due Process Consultation	<p>Enhancing due process consultation with major assurance practitioners and user constituent groups² on specific issues relating to the auditing and assurance standards, especially consultation relating to due process documents, by:</p> <ul style="list-style-type: none"> a. Identifying and implementing innovative, targeted consultation methods that are high value-added but relatively low-effort from the constituents' point of view; and b. Proactively engaging with relevant constituent groups about specific technical issues or matters being considered domestically or internationally.
Action 4.2: Undertaking On-Going Dialogue	<p>Undertaking an on-going dialogue with relevant constituent groups across all sectors on general matters relating to auditing and assurance standards, including changes resulting from the evolving nature of the audit market by:</p> <ul style="list-style-type: none"> a. Meeting with major constituent groups on a rolling basis as part of the NZAuASB's regular meetings; b. Taking opportunities to meet with major constituent groups in other fora, including at events hosted by those groups; and c. Maintaining strong working relationships at the operational level with key constituent groups.
Action 4.3: Improving Engagement Relating to Other Assurance Reports	<p>Seeking to improve its engagement with assurance practitioners and (particularly) users of Other Assurance Reports (i.e. assurance engagements other than audits and reviews of historical financial statements) by:</p> <ul style="list-style-type: none"> a. Developing and maintaining a constituency database identifying these users and assurance practitioners; b. Specifically targeting this group when consulting about relevant standards using customised communication approaches.
Action 4.4: Improving Engagement with Small Assurance Practitioners	<p>Seeking to improve its engagement with assurance practitioners that are small firms and sole practitioners, by:</p> <ul style="list-style-type: none"> a. Developing and maintaining a constituency database identifying these assurance practitioners; b. Specifically targeting this group when consulting about relevant standards using customised communication approaches.
<i>Awareness raising activities: ensuring assurance practitioners understand the auditing and assurance standards they have to apply when performing assurance engagements required by law.</i>	
Action 4.5: Promoting Understanding of Other	<p>Undertaking activities to promote an increased understanding of the requirements of Other Assurance Standards and the</p>



² CAANZ, CPA, FMA, IOD, NZX and others



Assurance Engagements	<p>engagements they apply to, by:</p> <p>Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate that help raise awareness of assurance practitioners and users about what comprises Other Assurance engagements and the standards that apply to those engagements.</p>
Action 4.6: Promoting Greater Understanding of the Purpose of Audits and Reviews	<p>Undertaking activities to promote an increased understanding by assurance users of the purpose of audit and review engagements by:</p> <ol style="list-style-type: none"> Actively encouraging, facilitating and supporting other relevant organisations to help them educate their members on the purpose of audit and review engagements; Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate to help raise awareness of assurance users and those charged with governance in the general constituency about the purpose of audit and review engagements, with a particular emphasis on the NFP sector.
Action 4.7: Promoting Understanding of the New Auditor Reporting Requirements	<p>Undertaking activities to promote an understanding of the IAASB's new auditor reporting requirements as they apply to New Zealand reporting entities, by:</p> <ol style="list-style-type: none"> Actively encouraging, facilitating and supporting other relevant organisations where appropriate to help them ensure their members understand the new auditor reporting requirements; Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate that help raise awareness of assurance users and those charged with governance about the new auditor reporting requirements.
<u>Action 4.8: Promoting Understanding of the new restructured Code of Ethics</u>	<p><u>Undertaking activities to promote an understanding of the new restructured Code of Ethics that apply to assurance practitioners, by:</u></p> <ol style="list-style-type: none"> <u>Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate to help raise awareness of assurance practitioners about the new restructured Code of Ethics.</u>
<p><i>Sector facilitation: encouraging, facilitating and supporting other relevant organisations to provide appropriate training and professional development activities relating to financial reporting; and working with other agencies to ensure the linkages between the work of relevant agencies in the financial reporting area are identified and gaps addressed.</i></p>	
Action 4.9: Promoting Understanding of the Factors that Affect Audit Quality	<ol style="list-style-type: none"> Actively encouraging, facilitating and supporting other relevant organisations where appropriate to help them ensure their members understand the factors that affect audit quality;


	b. Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate that inform all participants in the external reporting supply chain about the factors that affect audit quality.
Action 4.10: Facilitating the enhancement of audit quality	<p><u>Facilitating discussions to determine if there is a need to develop a best practice guide for audit committees in New Zealand, by:</u></p> <p>a. <u>Approaching other relevant participants in the reporting chain (for example MBIE, IoD, NZX, FMA and the audit firms) to determine if there is an appetite for the joint development of a best practice guide for audit committees</u></p>

4. NZAuASB Strategic Action Plan Summary

The NZAuASB's planned strategic actions are summarised in the table below.

	Specific Strategy	Action
	Specific Strategy 1: Maintain & Enhance Existing Standards – Part A: Maintain Existing Suites of Standards (Business as Usual) <u>The primary responsibility of the NZAuASB is to maintain and enhance the existing suite of auditing and assurance standards (including professional and ethical standards for assurance practitioners); and to continue the convergence and harmonisation approach (where relevant) for auditing and assurance standards.</u>	Action 1A.1: Contributing to International Due Process
		Action 1A.2: Maintaining New Zealand Standards
		Action 1A.3: Monitoring the Assurance Environment
	Specific Strategy 1: Maintain & Enhance Existing Standards – Part B: Address Critical Issues <u>This strategy is to address any deficiencies or gaps in existing standards that are critical to user-needs and the quality of financial reporting. The actions required under this strategy are to (a) identify critical issues; and (b) undertake appropriate actions to address those critical issues within a reasonable timeframe.</u>	Action 1B.1: Developing Guidance on Assurance on Non-Financial Information
		Action 1B.2: Developing an Assurance Standard on the Examination of Prospective Information
		Action 1B.3: Developing an Auditing Standard on Auditing of Service Performance Information
		Action 1B.4: Consider what further guidance is needed on the use of the XRB auditing and assurance standards and relevant assurance products and develop guidance where

		identified.
		Action 1B.5: Developing a Review Standard on Reviewing of Service Performance Information
		Action 1B.6: Developing an Engagement Standard/Guidance for smaller NFPs to better meet the needs of users, as informed by research completed in 2016-2017.
		Action 1B.7 : Perform a post implementation review jointly with the AUASB on the Compliance Engagement Standard
		Action 1B.8: Developing guidance or amending NZ SRE 2410 <i>Review of Financial Statements Performed by the Independent Auditor of the Entity</i>
		Action 1 B9: Review the compelling reason test
	Specific Strategy 2: Undertake User-Needs Research <u>A key objective of the XRB is to ensure that auditing and assurance standards are based on a user-needs approach i.e. the assurance reports required by those standards provide the level of assurance and information required by users of those assurance reports for accountability and decision-making purposes.</u> <u>This strategy involves undertaking deliberate, organised research into needs of the various users of NZAuASB standards as a basis for considering enhancements to the NZAuASB's standards in the future, and to help inform efforts to influence the work of the international standard setting boards.</u>	Action 2.1 Undertake user needs research as appropriate
	Specific Strategy 3: Influence the International Boards <u>The NZAuASB strategy is to seek to influence the work of the International Auditing and Assurance Standards Board (IAASB) and the International</u>	Action 3.1: Building Relationships with the IAASB
		Action 3.2: Increasing the International Visibility of the NZAuASB
		Action 3.3: Supporting Lyn Provost in

	<u>Ethics Standards Board for Accountants (IESBA) during the early stages of standards development, through the establishment of “influencing strategies” specific to each international board.</u>	her role as IAASB member.
		Action 3.4: Building Relationships with the IESBA
	Specific Strategy 4: Enhance Constituency Engagement and Support <u>A key aspect of the NZAuASB’s standard setting strategy is to ensure that standards are developed with constituents in a collaborative manner, through outreach, awareness raising activities and sector facilitation. This strategy also includes maintaining relationships with key stakeholder groups to monitor any emerging issues.</u>	Action 4.1: Enhancing Due Process Consultation
		Action 4.2: Undertaking On-Going Dialogue
		Action 4.3: Improving Engagement Relating to Other Assurance Reports
		Action 4.4: Improving Engagement with Small Assurance Practitioners
		Action 4.5: Promoting Understanding of Other Assurance Engagements
		Action 4.6: Promoting Greater Understanding of the Purpose of Audits and Reviews
		Action 4.7: Promoting Understanding of the New Auditor Reporting Requirements
		Action 4.8: Promoting Understanding of the new restructured Code of Ethics
		Action 4.9: Promoting Understanding of the Factors that Affect Audit Quality
		Action 4.10: Facilitating the enhancement of audit quality

APPENDIX A: Summary of the XRB's Strategic Priorities for the 2018-2023 Period

The XRB's strategies aim to contribute to building trust and confidence in the reporting by New Zealand organisations across all sectors³.

In the period from 1 July 2018 to 30 June 2023, the XRB plans to further develop the standards frameworks (including accounting and auditing & assurance standards⁴) to ensure they continue to be fit-for-purpose for the future. The XRB will focus on developing the User-needs Framework to ensure it is *A User-needs Framework for New Zealand's Wellbeing* and that the XRB's standards frameworks (and standards) meet user-needs and continue to:

- engender confidence in New Zealand financial reporting;
- assist New Zealand entities to compete; and
- enhance entities' accountability to New Zealand stakeholders,

thereby contributing to sustainable and inclusive economic goals and the wellbeing of New Zealanders.

Strategic Priorities – 2018-2023

The XRB's outcome goal in the period 2018-2023 will be achieved through several specific strategies, as set out below:

Overarching Strategy – Broad strategic approach	
<ul style="list-style-type: none">• Maintaining the existing financial reporting strategy including the two-sector, multi-standards, multi-tier Accounting Standards Framework• Continuing, as appropriate, the convergence and harmonisation approach for both accounting and auditing & assurance standards• Responding to the rapidly changing international environment and external reporting landscape	
Specific Strategy	To be achieved by....
Specific Strategy 1: Maintain and Enhance Existing Standards	<p>Enduring policy of sector-specific standards and Tier Structure.</p> <p>Maintaining a financial reporting strategy and standards frameworks that are:</p> <ul style="list-style-type: none">• Reliable and require infrequent changes;• Consistent with legislative frameworks; and• Responsive to legislative changes and stakeholder feedback. <p>Appropriate policy of international convergence/harmonisation.</p> <p>Maintaining existing accounting and auditing & assurance standards (and associated pronouncements) so that:</p> <ul style="list-style-type: none">• They are of high quality;• They remain consistent with international standards, as appropriate; and• There is local relevance and acceptance. <p>Enhancing existing accounting and auditing & assurance standards (and associated pronouncements) by:</p>

³ The underlying foundations of the XRB's strategic plan are set out in detail in the XRB's [Strategic Plan 1 July 2014 to 30 June 2019](#) and in subsequent Strategic Plans.

⁴ Auditing & assurance standards, including ethics standards.

	<ul style="list-style-type: none"> Identifying and addressing any New Zealand-specific deficiencies or gaps; and Expanding, where necessary, the XRB's legal mandate in relation to the issue of standards, for example, in relation to pronouncements on EER. <p>Ensuring transparent due process and consultation.</p> <p>Reviewing the existing "standard taker" policy, understanding the ramifications of change and discussing with policy makers.</p>
Specific Strategy 2: Undertake User-needs Research	<p>Undertaking organised research into the financial and non-financial information needs of users of our standards:</p> <ul style="list-style-type: none"> as a basis for enhancing the financial reporting framework or specific standards; to inform efforts to influence the work of the international standard setting boards; to respond to developments in wider corporate reporting; and to provide thought leadership. <p>Undertaking a post-implementation review of the standards frameworks in the period 2019-2020, including the costs and benefits aspects of the standards frameworks.</p> <p>Investigating the hosting of "labs" or "think tanks" to bring fresh thinking for consideration.</p>
Specific Strategy 3: Influence the International Boards	<p>Seeking to influence the work of the international boards during appropriate stages of standards development to ensure high quality global standards that are applicable in New Zealand:</p> <ul style="list-style-type: none"> Using "influencing strategies" specific to each international board; and By participating, building relationships, and, where appropriate, being represented on international boards. <p>Monitoring and responding to major disruptions and developments in the international standard setting structures and environment, particularly in the audit market, and ensuring that stakeholders are well informed.</p> <p>Maintaining and enhancing regional relationships with like-minded countries, as a contingency plan in the event of a return to national standard setting or a move away from principles-based standards.</p> <p>Re-considering the most effective investment of resources in respect of our influencing strategies, whether this be at the commencement of the standard setting process, the end of the standard setting process or working more closely with regional groups.</p>
Specific Strategy 4: Enhance Constituency Engagement and Support	<p>Developing standards in a collaborative manner with the constituency by:</p> <ul style="list-style-type: none"> Implementing engagement strategies to enhance the depth and breadth of constituency engagement; and Increasing awareness raising activities, including through a communication strategy for social media. <p>Promoting the awareness, understanding and implementation of EER among New Zealand constituents by:</p> <ul style="list-style-type: none"> adopting a proactive leadership approach to EER, giving consideration to investor versus broader stakeholder requirements; considering and implementing a strategy for EER in response to user demands; and

	<ul style="list-style-type: none"> adopting a collaborative approach with other key stakeholders to EER. <p>Working with other agencies, including other standard-setters, to ensure external reporting and assurance gaps are identified and addressed.</p> <p>Providing a thought leadership role involving bold thinking, being proactive and facilitating meetings with key stakeholders to make a difference.</p> <p>Encouraging, facilitating and supporting other relevant organisations to provide appropriate training and professional development activities relating to external reporting.</p>
Specific Strategy 5: Maintain Capability within a Financially Prudent Organisation	<p>Maintaining a high-performance culture to achieve the XRB's outcome goals in a rapidly changing environment.</p> <p>Operating in a financially prudent manner.</p> <p>Maintaining the level of capability needed to deliver the outputs.</p> <p>Reviewing at least annually the External Reporting Advisory Panel (XRAP) membership to ensure an appropriate representation of all stakeholders.</p> <p>Strengthening, widening and improving the relationship matrix.</p> <p>Ensuring prompt commencement of the preparations for the post-implementation review of the standards framework in 2019/2020.</p> <p>Considering use of a digital specialist or specialised advisory group to provide timely and expert advice on technological challenges to XRB's work.</p> <p>Strengthening the risk register for wider issues affecting the XRB.</p>

Summarised NZAuASB Strategic Action Plan 2018-2021: Indicative Resourcing

Strategic Plan Strategy	NZAuASB Actions		
Specific Strategy 1: Maintain and Enhance Existing Standards – Part A: Maintain Existing Suites of Standards (Business as Usual)			
Monitoring	NZAuASB Action 1A.3: Monitoring the Assurance Environment	Timing: Ongoing	Resource: Within existing capacity
International Due Process	NZAuASB Action 1A.1: Contributing to International Auditing and Assurance Standards Due Process	Timing: Ongoing	Resource: Within existing capacity
Maintenance	NZAuASB Action 1A.2: Maintaining New Zealand Auditing and Assurance Standards	Timing: Ongoing	Resource: Within existing capacity
Specific Strategy 1: Maintain and Enhance Existing Standards – Part B: Address Critical Issues			
For-Profit Entities	NZAuASB Action 1B.1: Developing Guidance on Assurance on Non-Financial Information	Timing: Later years	Resource: Significant within existing capacity
General	NZAuASB Action 1B.2: Developing an Assurance Standard on the Examination of Prospective Information	Timing: This financial year ¹	Resource: Significant within existing capacity
PBE Entities	NZAuASB Action 1B.3: Developing an Auditing Standard on Auditing of Service Performance Information	Timing: Underway	Resource: Moderate within existing capacity
General	NZAuASB Action 1B.4: Consider what further guidance is needed on the use of the XRB auditing and assurance standards and relevant assurance products	Timing: This financial year	Resource: Moderate within existing capacity
PBE Entities	NZAuASB Action 1B.5: Developing a Review Standard on Reviewing Service Performance Information	Timing: This financial year ²	Resource: Significant within existing capacity
PBE Entities	NZAuASB Action 1B.6: Developing an Engagement Standard/Guidance for smaller NFPs to better meet the needs of users, as informed by research completed in 2016-2017.	Timing: This financial year. ³	Resource: Significant within existing capacity
General	NZAuASB Action 1B.7: Perform a post implementation review on the use of the Compliance Engagement Standard	Timing: This financial year.	Resource: Moderate within existing capacity
General	NZAuASB Action 1B.8: Developing guidance or amending NZ SRE 2410 Review of Financial Statements Performed by the	Timing: This financial year.	Resource: Moderate within existing capacity

¹ Delayed by 6 months

² Delayed by 16 months

³ Delayed by 6 months

	Independent Auditor of the Entity		
General	NZAuASB Action 1B.9: Review the compelling reason test	Timing: This financial year	Resource: within existing capacity
General	NZAuASB Action 1B.10: Perform a post implementation review of the SPI auditing standard	Timing: Later years- post 2018-2023	Resource: Moderate within existing capacity
Strategic Plan Strategy	NZAuASB Actions		
Specific Strategy 2: Undertake User-Needs Research			
For-Profit Users	NZAuASB Action 2.1: Researching Assurance Needs of Users of Non-Public Interest Entities Reports	Timing: Completed	
NFP Users	NZAuASB Action 2.2: Researching the Demand for Simple Assurance for Small NFPs	Timing: Completed	
General	NZAuASB Action 2.3: Obtaining a better understanding about the integrity of the application of ISAE(NZ) 3000 (Revised)	Timing: Completed	
Strategic Plan Strategy	NZAuASB Actions		
Specific Strategy 3: Influence the International Boards			
IAASB & IESBA	NZAuASB Action 3.1: Building Relationships with the IAASB	Timing: Ongoing	Resource: Chief executive and moderate within existing capability
	NZAuASB Action 3.2: Increasing the International Visibility of the NZAuASB	Timing: Ongoing	Resource: Within existing capability
	NZAuASB Action 3.3: Building Relationships with the IESBA	Timing: Ongoing	Resource: Chief executive and within existing capability
	Action 3.4: Supporting Lyn Provost in her role as IAASB member	Timing: Ongoing	Resource: Moderate within existing capacity
Strategic Plan Strategy	NZAuASB Actions		
Specific Strategy 4: Enhance Constituency Engagement and Support			
Due Process Engagement	NZAuASB Action 4.1: Enhancing Auditing and Assurance Standards Due Process Consultation	Timing: Ongoing	Resource: Within existing capability

	NZAuASB Action 4.3: Improving Engagement Relating to Other Assurance Reports	<i>Timing:</i> Ongoing	<i>Resource:</i> Within existing capability
	NZAuASB Action 4.4: Improving Engagement with Small Assurance Practitioners	<i>Timing:</i> Ongoing	<i>Resource:</i> Within existing capability
<i>General Engagement</i>	NZAuASB Action 4.2: Undertaking On-Going Dialogue with Auditing and Assurance Standards Constituent Groups	<i>Timing:</i> Ongoing	<i>Resource:</i> Within existing capability
<i>Constituency Education</i>	NZAuASB Action 4.5: Promoting Understanding of Other Assurance Engagements	<i>Timing:</i> Ongoing	<i>Resource:</i> Within existing capacity
	NZAuASB Action 4.6: Promoting Greater Understanding of the Purpose of Audits and Reviews	<i>Timing:</i> This financial year, then ongoing	<i>Resource:</i> Within existing capacity
	NZAuASB Action 4.7: Promoting Understanding of the New Auditor Reporting Requirements	<i>Timing:</i> Underway	<i>Resource:</i> Within existing capacity
	NZAuASB Action 4.8: Promoting Understanding of the New NOCLAR Requirements	<i>Timing:</i> Completed, monitoring ongoing	<i>Resource:</i> within existing capacity
	NZAuASB Action 4.8: Promoting Understanding of the new restructured Code of Ethics	<i>Timing:</i> This financial year	<i>Resource:</i> within existing capacity
	NZAuASB Action 4.9: Promoting Understanding of the Factors that Affect Audit Quality	<i>Timing:</i> Ongoing	<i>Resource:</i> within existing capacity
<i>Sectoral Facilitation</i>	NZAuASB Action 4.10: Facilitating the enhancement of audit quality	Timing: This financial year	<i>Resource:</i> Moderate within existing capacity

Summarised NZAuASB Strategic Action Plan 2018-2023: Indicative Timing

Action	July 2018 – June 2019	July 2019 – June 2020	July 2020 – June 2021	July 2021- June 2022	July 2022- June 2023
Specific Strategy 1: Maintain and Enhance Existing Standards – Part A Business as Usual: Monitoring					
NZAuASB Action 1A.1: Contributing to International Auditing and Assurance Standards Due Process	Ongoing				
Specific Strategy 1: Maintain and Enhance Existing Standards – Part A Business as Usual: International Due Process					
NZAuASB Action 1A.2: Maintaining New Zealand Auditing and Assurance Standards	Ongoing				
Specific Strategy 1: Maintain and Enhance Existing Standards – Part A Business as Usual: Maintenance					
NZAuASB Action 1A.3: Monitoring the Assurance Environment	Ongoing				
Specific Strategy 1: Maintain and Enhance Existing Standards – Part B: Address Critical Issues: For-Profit Entities					
NZAuASB Action 1B.1: Developing Guidance on Assurance on Non-Financial Information					
Specific Strategy 1: Maintain and Enhance Existing Standards – Part B: Address Critical Issues: Public Benefit Entities					
NZAuASB Action 1B.3: Developing an Auditing Standard on Auditing of Service Perf. Information					
Specific Strategy 1: Maintain and Enhance Existing Standards – Part B: Address Critical Issues: General					
NZAuASB Action 1B.2: Developing an Assurance Standard on the Examination of Prospective Information	¹				
NZAuASB Action 1B.4: Adopting the revised IAASB standard on					

¹ Completion date extended by 6 months

Agreed Upon Procedures ²					
Action	July 2018 – June 2019	July 2019 – June 2020	July 2020 – June 2021	July 2021-June 2022	July 2022 – June 2023
NZAuASB Action 1B.4: Consider what further guidance is needed on the use of the XRB auditing and assurance standards and relevant assurance products and develop guidance where identified					
NZAuASB Action 1B.5: Developing a Review Standard on Reviewing Service Performance Information		³			
NZAuASB Action 1B.6: Developing an engagement standard/guidance for smaller NFPs	⁴				
NZAuASB Action 1B.7: Perform a post implementation review on the use of the Compliance Engagement Standard Service	⁵				

² Previously planned to develop domestic standard in 2017/18. Delay in obtaining mandate to issue AUP standard, so deleted action as will adopt international standard when released as part of business as usual

³ Previously planned to commence Feb 2018. Commencement delayed due to delay in completion of Auditing Standard. To commence 2nd half 2018/19 and completion date extended to June 2020 (previously Feb 2019).

⁴ Previous planned timing was between Dec 2017 and June 2019. Completion extended by 6 months to Dec 2019.

⁵ New action identified to perform a post implementation review to determine if further guidance is needed. Replaces previous action to develop Guidance.

Action	July 2018 – June 2019	July 2019 – June 2020	July 2020 – June 2021	July 2021-June 2022	July 2022 – June 2023
NZAuASB Action 1B.8: Developing guidance or amending NZ SRE 2410 <i>Review of Financial Statements Performed by the Independent Auditor of the Entity</i>	6				
NZAuASB Action 1B.10: To consider developing guidance for Audit Committees. ⁷					
NZAuASB Action 1B.9: Review the compelling reason test	8				
NZAuASB Action 1B10: Perform a post implementation review of the SPI audit standard 3 years post implementation.	9				

⁶ Previously planned to complete in 2017/18. Has been delayed due to other priorities.

⁷ Replaced by new action under strategy 4, Facilitating the enhancement of audit quality

⁸ New action identified.

⁹ New action identified. To commence 2023/24. Not within this 5-year plan 2018-2023.

Action	July 2018 – June 2019	July 2019 – June 2020	July 2020 – June 2021	July 2021-June 2022	July 2022 – June 2023
Specific Strategy 2: Undertake User-Needs Research: For-Profit Users					
XRB Action 2.2: Researching Information Needs of Users of For-Profit Tier 2 Entity Reports	Completed – no further action required				
XRB Action 2.3: Researching Non-Financial Information Needs of Users in the For-Profit Sector					
NZASB Action 2.1: Researching Information Needs of Users of Tier 2 For-Profit Financial Reports					
NZAuASB Action 2.1: Researching Assurance Needs of Users of Non-Public Interest Entities Reports					
Specific Strategy 2: Undertake User-Needs Research: Specific Issues					
NZAuASB Action 2.2: Obtaining a better understanding about the integrity of the application of ISAE (NZ) 3000(Revised)	Completed – no further action required				

Action	July 2018 – June 2019	July 2019 – June 2020	July 2020 – June 2021	July 2021-June 2022	July 2022-June 2023
Specific Strategy 3: Influence the International Boards: IAASB & IESBA					
NZAuASB Action 3.1: Building Relationships with the IAASB	Ongoing				
NZAuASB Action 3.3: Building Relationships with the IESBA	Ongoing				
NZAuASB Action 3.2: Increasing the International Visibility of the NZAuASB	Ongoing				
Specific Strategy 4: Enhance Constituency Engagement and Support: Due Process Engagement					
NZAuASB Action 4.1: Enhancing Auditing and Assurance Standards Due Process Consultation	Ongoing				
NZAuASB Action 4.3: Improving Engagement Relating to Other Assurance Reports	Ongoing				
NZAuASB Action 4.4: Improving Engagement with Small Assurance Practitioners	Ongoing				
Specific Strategy 4: Enhance Constituency Engagement and Support: General Engagement					
NZAuASB Action 4.2: Undertaking On-Going Dialogue with A&A Standards Constituent Groups	Ongoing				
Specific Strategy 4: Enhance Constituency Engagement and Support: Constituency Awareness Raising					
NZAuASB Action 4.5: Promoting Understanding of Other Assurance Engagements	Ongoing				
NZAuASB Action 4.6: Promoting Greater Understanding of the Purpose of Audits and Reviews	Ongoing				

Action	July 2018 – June 2019	July 2019 – June 2020	July 2020 – June 2021	July 2021-June 2022	July 2022-June 2023
NZAuASB Action 4.7: Promoting Understanding of the New Auditor Reporting Requirements					
NZAuASB Action 4.8: Promoting Understanding of the New NOCLAR Requirements¹⁰					
NZAuASB Action 4.8: Promoting understanding of the new restructured Code of Ethics	¹¹				
Specific Strategy 4: Enhance Constituency Engagement and Support: Sectoral Facilitation					
NZAuASB Action 4.9: Promoting Understanding of the Factors that Affect Audit Quality	Ongoing				
NZAuASB Action 4.10: Facilitating the Enhancement of Audit Quality	¹²				

¹⁰ Deleted this action as completed and continue to monitor as part of action 1.3.

¹¹ New action identified.

¹² New action identified to replace previous action to develop Audit Committee Guidance. New action identified to consider approaching other relevant participants in the reporting chain to determine if there is an appetite for the joint development of a best practice guide for audit committees in New Zealand

Specific Strategy 1: Maintain Existing Suites of Standards

Key: Green – ongoing activity and on track Orange – action is work in progress and on track Red – no action taken			
NZAuASB Action 1A.1: Contributing to International Auditing and Assurance Standards Due Process	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<i>The NZAuASB will actively contribute to the "due process" activities of the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA). These activities relate to the development or amendment of international standards.</i>			
The Action will comprise:			
a. Ensuring assurance practitioners and relevant users of assurance reports are aware of IAASB and IESBA due process documents and encouraging them to make submissions directly to the international boards and to the NZAuASB;	Ongoing	<ul style="list-style-type: none">• Issue communiques when international documents issued• Organise consultation events as appropriate	
b. Responding, as appropriate, to IAASB and IESBA due process documents (consultation documents, discussion papers and exposure drafts) and doing so in conjunction with the Australian Auditing and Assurance Standards Board (AUASB) and Australian Accounting and Professional Ethical Standards Board (APESB) where appropriate;		<ul style="list-style-type: none">• Prepare comment letters• Liaise with AUASB in accordance with established protocol before letters finalised• Liaise with APESB to the extent considered appropriate in each case	

c. Participating, as appropriate, in roundtables and other face-to-face due process related meetings organised by the international boards.		<ul style="list-style-type: none"> Participate in events in NZ or Australia (or elsewhere on an exceptional basis) 	
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NZAuASB Action 1A.2: Maintaining New Zealand Auditing and Assurance Standards	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will amend the auditing and assurance standards (auditing standards, review engagement standards, other assurance standards) to ensure that the existing suites of standards are maintained on an on-going basis.</i></p> <p>The Action will comprise:</p>			
<p>a. Incorporating any auditing and assurance standards, or amendments to those standards, issued by the IAASB, to achieve convergence, and including working with the AUASB to ensure any changes are appropriately harmonised; and</p>	<p>Ongoing</p>	<ul style="list-style-type: none"> • Amend standards following due process as documents issued by IAASB • Liaise with AUASB in accordance with harmonisation process protocol 	
<p>b. Incorporating any professional and ethical standards for assurance practitioners, or amendments to those standards, issued by IESBA, including liaising with the APESB to ensure any changes are appropriately harmonised.</p>		<ul style="list-style-type: none"> • Amend standards following due process as documents issued by IESBA • Interact with APESB staff and Chair as appropriate • Observe some APESB meetings to build relationships with staff and the Board • Agree a communications protocol with the APESB • Develop harmonisation process protocol with APESB 	

		<ul style="list-style-type: none"> • Apply APESB harmonisation protocol 	
c. Respond as appropriate to any gaps /issues identified with the current suite of standards identified		<ul style="list-style-type: none"> • Develop an appropriate response where such matters are identified. 	
<u>d. Incorporating any amendments to international standards to domestic standards where applicable, including liaising with the AUASB.</u>		<ul style="list-style-type: none"> • <u>Amend standards following due process and agreed policy.</u> 	
NZAuASB Action 1A.3:	Timing	2018/19 Planned Actions	2018/19 Actual Actions
Monitoring the Assurance Environment			
<p><i>The NZAuASB will monitor the wider assurance environment and consider the implications of any developing issues for New Zealand auditing and assurance standards.</i></p> <p>The Action will comprise:</p>			
a. Monitoring issues arising from the implementation of the current suite of standards and responding as appropriate;	Ongoing	<u>Continue to specifically monitor:</u> <ul style="list-style-type: none"> • <u>implementation of new auditor reporting for FMC reporting entities</u> • <u>implementation of NOCLAR</u> • <u>implementation of long association provisions</u> • <u>auditing of SSPs</u> • Passive monitoring via media, public sources, and relationship contacts 	

		<ul style="list-style-type: none"> • Monitor modified auditor reports and report half yearly to Board 	
b. Monitoring issues or gaps with the current suite of standards and responding as appropriate.	Ongoing	<ul style="list-style-type: none"> • <u>Take action as appropriate as matters arise during the year</u> 	
c. Tracking local and international research projects and considering the implications for the New Zealand auditing and assurance standards;	Ongoing	<ul style="list-style-type: none"> • <u>Monitor projects, specifically:</u> <ul style="list-style-type: none"> - <u>global extended external reporting developments</u> - <u>academic research</u> - <u>use of data analytics and artificial intelligence in auditing;</u> - <u>auditing for SMEs</u> 	
d. Monitoring results from QA reviews conducted locally and internationally and considering the implications for New Zealand auditing and assurance standards;	Ongoing	<ul style="list-style-type: none"> • Director continue to participate at FMA Audit Oversight Committee meetings and report as necessary to the Board • Analyse results of QA reviews for standards issues. • Liaise with FMA on reviews conducted. 	

e. Contributing to government policy work relating to auditing and assurance and other related services standards	Ongoing	<ul style="list-style-type: none"> • Interact with MBIE and other agencies as requested by them, or as identified as necessary 	
f. <u>Building relationships and liaising with other relevant NSSs on matters of mutual interests (specifically on the use of data analytics and audit of SMEs)</u>		<ul style="list-style-type: none"> • Consider matters raised at NSS meetings and take appropriate actions if any implications for NZ standards • Interact with APESB at NSS meetings and at least annually through Chair-Chair and senior staff level contact • Have 6-monthly phone catch up with Canadian ethics NSS chair. • <u>Follow up NSS meeting contacts as appropriate</u> • <u>Have 6-monthly catch ups with Canadian ASB and AUASB</u> • <u>Set up regular catch ups with established NSS contacts from South Africa, Hong Kong, Singapore</u> • <u>Build relationships with NSS contact from China with view to establish regular catch ups.</u> 	

		<ul style="list-style-type: none"> • <u>Continue to work with the AUASB in setting up the NSS collaborative</u> 	
g. <u>Monitoring the assurance environment for changes coming out of the Monitoring Group</u>		<ul style="list-style-type: none"> • <u>Monitor developments and consider if any action is required</u> 	
h. <u>Keeping a watching brief over the possible restructuring of firms and the impact on the assurance environment.</u>		<ul style="list-style-type: none"> • <u>Monitor developments and consider if any action is required</u> 	
i. <u>Monitoring the XRB EER project, contributing to the development of guidance as appropriate, and considering the implications for New Zealand auditing and assurance standards.</u>		<ul style="list-style-type: none"> • <u>Monitor developments and consider if any action is required</u> 	
j. <u>Monitoring activities and developments in the wider assurance standard setting space</u>		<ul style="list-style-type: none"> • <u>Monitor developments and consider if any action is required</u> 	

Specific Strategy 1: Address Critical Issues

NZAuASB Action 1B.2:	Timing	2018/19 Planned Actions	2018/19 Actual Actions
Developing an Assurance Standard on the Examination of Prospective financial information			
<p><i>The NZAuASB will develop an assurance standard for other assurance engagements involving the examination of prospective financial information.</i></p> <p>This action will comprise:</p>			

Developing the standard in accordance with the due process for domestic standards, ensuring harmonisation with the AUASB standard as appropriate.	Commence 2017/18 Complete 2018/19 2019/20	<ul style="list-style-type: none"> Approve <u>updated</u> project plan and Commence <u>continue</u> development of standard in accordance with the agreed project plan 	
NZAuASB Action 1B.3: Developing an Auditing Standard on Auditing Service Performance Information	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will develop an auditing standard on auditing service performance for Public Benefit Entities (PBEs).</i></p> <p>The Action will comprise:</p>			
Developing the standard in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.	Whole year	<ul style="list-style-type: none"> Develop SSP audit standard for exposure September 2017 <u>Issue limited review exposure</u> Issue <u>final</u> standard 	
NZAuASB Action 1B.5: Developing <u>Consider what further guidance is needed</u> on the use of the XRB auditing and assurance standards and relative assurance products, <u>and develop guidance where identified</u>	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will <u>consider what further guidance is needed</u> develop guidance that explain the difference between reasonable and limited assurance, as well as various assurance products that are available, and relevant standards to use, how to deal with unclear assurance requirements, and the correct terminology to use when setting assurance requirements in legislation and/or policies.</i></p> <p>The action will comprise:</p>			

Developing appropriate guidance.	Whole year.	<ul style="list-style-type: none"> Complete guidance for policy makers and legislators by 30-Dec 2017 <u>Consider if there is a need for further guidance on the use of the assurance standards.</u> Develop further guidance in accordance with the approved project plan. Include guidance on website Promote the guidance 	
NZAuASB Action 1B.6: Developing a review standard on reviewing service performance information	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will develop a review standard on reviewing service performance information for Public Benefit Entities (PBEs)</i></p> <p>The action will comprise:</p>			
Developing the standard in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.	<p>Commence 2nd half 2017-18 and complete 2018-19</p> <p><u>Commence 2nd half 2018-19 and complete 2019-20.</u></p>	<ul style="list-style-type: none"> Approve project plan and commence development of the engagement standard in accordance with the agreed project plan. 	

NZAuASB Action 1B.7: Developing an engagement standard/guidance for smaller NFPs	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will develop an engagement standard/guidance for smaller NFPs not required to have an audit or a review to better meet the needs of users, as informed by research completed in 2016-17.</i></p> <p>The action will comprise:</p>			
Developing the standard/guidance in accordance with the due process for domestic standards and in collaboration with the AUASB as appropriate.	Commence 2nd half of 2018 - 2018-2019 and complete in 2018 2019 - 2019 2020	<ul style="list-style-type: none"> Approve project plan and commence development of the engagement standard/guidance in accordance with the agreed project plan 	
NZAuASB Action 1B.98: <u>Consider if there is a need to Develop develop</u> guidance or amending NZ SRE 2410 <i>Review of Financial Statements Performed by the Independent Auditor of the Entity</i>	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will consider developing guidance or amending NZ SRE 2410 for the new auditor reporting requirements.</i></p> <p>This action will comprise:</p>			

Deciding whether to amend the standard or to only develop guidance, similar to guidance developed by the AUASB. Amending the standard in accordance with the due process for domestic standards or developing guidance similar to the AUASB guidance.	Whole year.	<ul style="list-style-type: none"> • <u>Discuss with practitioners from the big 4 firms the need for guidance/amendments to the standard</u> • <u>Depending on the outcome of the discussions, Consider consider issues paper and decide</u> whether to amend the standard, or to develop guidance. • <u>If required, a</u>Approve the project plan and amend the standard and/or develop the guidance in accordance with the approved project plan 	
NZAuASB Action 1B.10: Consider developing guidance for Audit Committees, similar to the audit committee practice guide recently issued in Australia.	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will consider whether to develop guidance for Audit Committees, similar to the guidance recently issued in Australia.</i></p> <p><i>This action will comprise:</i></p>			
Consider the guidance for Audit Committees recently published in Australia, and decide whether to develop similar guidance in New Zealand, in collaboration with other parties.	Commence 2nd half of 2017-2018 and complete	Consider issues paper and decide whether to develop similar guidance for New Zealand.	

	in 2018-2019	<ul style="list-style-type: none"> If decide to develop similar guidance, approve the project plan. Develop the guidance in accordance with the approved project plan. 	
<u>NZAuASB Action 1B.9</u> <u>Perform a post implementation review of the Compliance Engagement Standard</u>	<u>Timing</u>	<u>2018/19 Planned Actions</u>	<u>2018/19 Actual Actions</u>
<p><i><u>The NZAuASB will perform a post implementation review of the Compliance Engagement standard to determine if further guidance is needed.</u></i></p> <p><u>This action will comprise:</u></p>			
<u>Performing a post implementation review of the Compliance standard jointly with the AUASB.</u> <u>Considering if further application guidance is needed.</u>	<u>Whole year</u>	<ul style="list-style-type: none"> <u>Liaise with the AUASB and develop a joint project plan for the post implementation review</u> <u>Perform the post implementation review in accordance with the approved project plan</u> <u>Consider the results together with the AUASB and decide whether further application guidance is needed.</u> 	
<u>NZAuASB Action 1B.10</u> <u>Perform a review of the compelling reason test</u>	<u>Timing</u>	<u>2018/19 Planned Actions</u>	<u>2018/19 Actual Actions</u>

<p><u>The NZAuASB will perform a review of the compelling reason test, in collaboration with the AUASB, to determine if it remains fit for purpose</u></p> <p><u>This action will comprise:</u></p>			
<p><u>Performing a review of the compelling reason test together with the AUASB about any changes that may be needed</u></p>		<ul style="list-style-type: none"> <u>Staff to liaise with AUASB staff and to prepare a joint issues paper for the 2 Boards to consider at concurrent meetings.</u> <u>Both Boards to consider outcome of the respective meetings, and staff to jointly prepare an update for Boards to approve at subsequent meetings.</u> 	

Specific Strategy 2: Undertake User-Needs Research

NZAuASB Action 2.1 Researching Assurance Needs of Users of Non-Public Interest Entities Reports	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will research the assurance needs of users of assurance reports for entities that are not public interest entities (non-PIEs). The result of the research will be used as input into a future review of whether users' needs are appropriately met by the less stringent requirements for assurance for non-PIEs.</i></p> <p><i>This Action is an outsourced XRB Combined project and comprises:</i></p>			

a. Identifying the types of entities that make up the non-PIE population	Completed		
b. A literature review on user assurance needs for those types of entities	Completed		
c. An empirically-based analysis of the users of assurance reports of those types of entities and their assurance needs	to complete 1 st half 2017/18	<ul style="list-style-type: none"> To consider research findings and recommendations 	
NZAuASB Action 2.2: Obtaining a better understanding about the integrity of the application of ISAE (NZ) 3000(Revised)	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAUASB will complete its research to seek information about to what extent and how the XRB standards on assurance engagements are applied by assurance practitioners (including non-accountants) performing other assurance engagements in New Zealand. The results of the research will be used as a basis for considering enhancements to the NZAuASB's standards in the future, and to help inform efforts to influence the work of the international setting boards.</i></p> <p>The action comprises:</p>			
a. Identifying the types of assurance engagements other than audits and reviews, assurance practitioners conduct in New Zealand in accordance with or with reference to the XRB assurance standards	Completed 2016/17.		
b. Analysing to what extent and how the XRB assurance standards are applied, and whether they adequately address the assurance requirements.	To complete 1st half of 2017/18.	<ul style="list-style-type: none"> To consider research findings and recommendations 	

Specific Strategy 3: Influence the International Boards

NZAuASB Action 3.1: Building Relationships with the IAASB	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will seek to build and maintain relationships with IAASB members and staff.</i></p> <p>The Action will comprise:</p>			
a. Attending relevant meetings and events (including National Standard Setters meetings);	Ongoing	<ul style="list-style-type: none"> • <u>Chair and Director to attend NSS meetings</u> • Director to attend IAASB meetings as Technical Advisor (TA) to Lyn Provost • Chair to observe IAASB meetings in conjunction with NSS meeting or otherwise as appropriate 	
b. Taking opportunities to meet with IAASB members and staff;		<ul style="list-style-type: none"> • <u>Interact with key staff and Chair as appropriate</u> • <u>NZAuASB representatives and staff to attend the NSS meeting in Sydney in Nov.</u> 	

c. Fostering relationships with Australasian representatives on the IAASB and those who are involved in relevant working groups;		<ul style="list-style-type: none"> • Support Lyn Provost as IAASB member (see 3,3) and interact regularly with Fiona Campbell at IAASB meetings and on specific topics as required • Work with AUASB at chair and staff level to influence international agenda. • Explore possibility of Regional NSS meetings 	
d. Hosting IAASB members and staff in visits to New Zealand as appropriate.		<ul style="list-style-type: none"> • Host IAASB members and staff as appropriate 	
e. <u>Collaborating with other NSSs to better influence the IAASB agenda and other global initiatives</u>		<ul style="list-style-type: none"> • <u>Director to liaise with IAASB Deputy Director and AUASB Director on NSS collaboration</u> • <u>Chair and Director to work with the AUASB Chair and Director to arrange regional NSS meetings and other NSS initiatives</u> • <u>Participate in NSSs collaboration events.</u> 	
NZAuASB Action 3.2:	Timing	2018/19 Planned Actions	2018/19 Actual Actions

Increasing the International Visibility of the NZAuASB			
<p><i>The NZAuASB will take advantage of opportunities to increase its visibility in the international arena so as to illustrate its ability to contribute to the work of the IAASB in a constructive and high quality way.</i></p> <p>The Action will comprise:</p>			
a. Volunteering to present at the NSS meetings on New Zealand projects or with the AUASB on joint projects; and	Ongoing	<ul style="list-style-type: none"> Identify possible topic to present on at NSS in May 2018<u>2019</u> 	
b. Identifying an appropriate, mutually beneficial IAASB project and contributing technical resources in support of that project.	Ongoing	<ul style="list-style-type: none"> Follow up discussions initiated with IAASB to support EER project. Contribute resources to other mutual beneficial projects as opportunities arise, for example AUPs, <u>Quality Control standards</u> and scalability of ISAs for SMEs 	
NZAuASB Action 3.3: Supporting Lyn Provost in her role as IAASB member	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will provide support to Lyn Provost in her role as IAASB member.</i></p> <p>The Action will comprise:</p>			
Providing support to Lyn Provost	Ongoing	<ul style="list-style-type: none"> Director to attend IAASB meetings as Technical Advisor (TA) to Lyn Provost 	

		<ul style="list-style-type: none"> • Invite Lyn Provost to Board meetings • Establish Technical Advisory Group and arrange <u>Arrange meetings with the Technical Advisory Group</u> to receive input before each IAASB meeting • Arrange high-level discussions between Lyn Provost and NZAuASB when appropriate (for example, at the outset of the response process on ISA 315 review). 	
NZAuASB Action 3.4: Building Relationships with the IESBA	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will seek to build relationships with IESBA members and staff.</i></p> <p>The Action will comprise:</p>			
a. Attending relevant meetings and events (including NSS meetings);	Ongoing	<ul style="list-style-type: none"> • Senior Project Manager to attend IESBA meeting in Dec 2017 • <u>Chair and Director to attend NSS meeting</u> • Chair to observe IESBA meetings in conjunction with NSS meeting or otherwise as appropriate 	

b. Taking opportunities to meet with IESBA members and staff; and		<ul style="list-style-type: none"> Interact with key staff and Chair as appropriate Secondment of Senior Project Manager to IESBA during Dec and January. 	
c. Fostering relationships with Australian representatives on the IESBA.		<ul style="list-style-type: none"> Build relationship with Australian IESBA member – Invite to a NZAuASB meeting. 	

Specific Strategy 4: Enhance Constituency Engagement and Support

NZAuASB Action 4.1: Enhancing Auditing and Assurance Standards Due Process Consultation	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will seek to enhance consultation with major assurance practitioners and user constituent groups on specific issues relating to the auditing and assurance standards, especially consultation relating to due process documents.</i></p> <p>The Action will comprise:</p>			
a. Identifying and implementing innovative, targeted consultation methods that are high value-added but relatively low-effort from the constituents' point of view; and	Ongoing	<ul style="list-style-type: none"> Continue current due process engagement methods Develop new communications & engagement approach that reflects different target groups Implement the XRB's communication strategy for social media when developed. 	

b. Proactively engaging with relevant constituent groups about specific technical issues or matters being considered domestically or internationally.		<ul style="list-style-type: none"> • Present updates on Auditing and Assurance standards to accounting, auditing, legal, and director community audiences • Promote other Topics as arise • Identify and engage with relevant groups about major new exposure drafts and standards. 	
NZAuASB Action 4.2: Undertaking On-Going Dialogue with Auditing and Assurance Standards Constituent Groups	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will undertake an on-going dialogue with relevant constituent groups across all sectors on general matters relating to auditing & assurance standards, including changes resulting from the evolving nature of the audit market.</i></p> <p>The Action will comprise:</p>			
a. Meeting with major constituent groups on a rolling basis as part of the NZAuASB's regular meetings;	Ongoing	<ul style="list-style-type: none"> • <u>Update and include liaison schedule as a standard agenda item</u> • Organise regular meetings <u>with key stakeholders identified on the liaison schedule</u> • <u>To target:</u> <ul style="list-style-type: none"> — practitioners from firms — IoD representatives — NZX representatives - FMA representatives 	

b. Taking opportunities to meet with major constituent groups in other fora, including at events hosted by those groups; and	Ongoing	<ul style="list-style-type: none"> Organise seminars & round tables Attend other fora Attend mid-tier forum 	
c. Maintaining strong working relationships at the operational level with key constituent groups.	Ongoing	<ul style="list-style-type: none"> Built relationships with key groups identified. 	
NZAuASB Action 4.3: Improving Engagement Relating to Other Assurance Reports	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will seek to improve its engagement with assurance practitioners and (particularly) users of Other Assurance Reports (i.e. assurance engagements other than audits and reviews of historical financial statements).</i></p> <p>The Action will comprise:</p>			
a. Developing and maintaining a constituency database identifying these users and assurance practitioners;	Ongoing	<ul style="list-style-type: none"> Maintain database 	
b. Specifically targeting this group when consulting about relevant standards using customised communication approaches.	Whole of year	<ul style="list-style-type: none"> Run targeted communications where relevant 	
NZAuASB Action 4.4: Improving Engagement with Small Assurance Practitioners	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will seek to improve its engagement with assurance practitioners that are small firms and sole practitioners.</i></p> <p>The Action will comprise:</p>			

a. Developing and maintaining a constituency database identifying these assurance practitioners;	Ongoing	<ul style="list-style-type: none"> • Maintain database 	
b. Specifically targeting this group when consulting about relevant standards using customised communication approaches.	Ongoing	<ul style="list-style-type: none"> • Run targeted communications where relevant, for example webinars, speaking opportunities at SMP's in-house training, surveys. • Liaise with professional bodies and raise awareness at special interest group meetings. • <u>Run targeted communications on the proposed changes to ISQC1, ISQC2, ISA 315, ISA 220 and on the finalised ISA 540(Revised)</u> • <u>Run targeted communications on the new restructured Code.</u> 	

NZAuASB Action 4.5:	Timing	2018/19 Planned Actions	2018/19 Actual Actions
Promoting Understanding of Other Assurance Engagements			
<i>The NZAuASB will undertake activities to promote an increased understanding of the requirements of Other Assurance Standards and the engagements they apply to.</i>			

The Action will comprise:			
Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate that inform assurance practitioners and users about what comprises Other Assurance engagements and the standards that apply to those engagements.		<ul style="list-style-type: none"> Promote guidance developed on the Compliance Engagement Standard Prepare "Fact Sheet"/Guidance on other assurance engagements Speaking engagements as opportunities arise Targeted meetings with users 	

NZAuASB Action 4.6: Promoting Greater Understanding of the Purpose of Audits and Reviews	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will undertake activities to promote an increased understanding by assurance users of the purpose of audit and review engagements</i></p> <p>This Action will comprise:</p>			
a. Actively encourage, facilitate and support other relevant organisations to help them educate their members on the purpose of audit and review; and	Ongoing	<ul style="list-style-type: none"> Liaise with Charity Services, CAANZ, CPA, IoD, RBNZ, Law Society. 	
b. Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate to help raise awareness of assurance users and those charged with governance in the general constituency about the purpose of audit and review engagements, with a particular emphasis on the NFP sector.	Ongoing	<ul style="list-style-type: none"> Speaking engagements as opportunities arise Second journal Articles for LawTalk XRBrief <u>NZAuASB targeted newsletters article</u> 	







		<ul style="list-style-type: none"> Publish and Promote guidance developed 	
NZAuASB Action 4.7: Promoting Understanding of the New Auditor Reporting Requirements	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<i>The NZAuASB will undertake activities to promote an understanding of the IAASB's new auditor reporting requirements as they apply to New Zealand reporting entities.</i> The Action will comprise:			
a. Actively encourage, facilitate and support other relevant organisations where appropriate to help them ensure their members understand the new auditor reporting requirements; and	Whole of year	<ul style="list-style-type: none"> Liaise with FMA, IoD, INFINZ, CAANZ (NZ), CPA, RBNZ and others. 	
b. Conducting seminars, presentations , speaking engagements and other awareness raising activities as appropriate to help raise awareness of assurance users and those charged with governance about the new auditor reporting requirements.		<ul style="list-style-type: none"> Speaking engagements as opportunities arise <u>Write a follow up article on the implementation of the new audit reporting requirements.</u> Complete joint project with the FMA on the reporting of KAM, in accordance with the agreed project plan. Promote results of joint FMA project 	-




NZAuASB Action 4.8: Promoting Understanding of the new NOCLAR Requirements	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The NZAuASB will undertake activities to promote an understanding of the new NOCLAR requirements that apply to assurance practitioners.</i></p> <p>The action will comprise:</p>			
a. Actively encourage, facilitate and support other relevant organisations where appropriate to help them ensure their members understand the new NOCLAR reporting requirements; and	Whole of year	<ul style="list-style-type: none"> • Liaise with IOD about doing an awareness raising session as part of the director education series. 	
b. Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate that inform assurance users and those charged with governance about the new NOCLAR reporting requirements.		<ul style="list-style-type: none"> • Include topic in annual update presentations • Speaking engagements as opportunities arise 	
<u>NZAuASB Action 4.8</u> <u>Promoting understanding of the revised and restructured Code of Ethics</u>	<u>Timing</u>	<u>2018/19 Planned Actions</u>	<u>2018/19 Actual Actions</u>
<p><u>The NZAUASB will undertake activities to promote an understanding of the revised and restructured Code of Ethics that apply to assurance practitioners.</u></p> <p><u>The action will comprise:</u></p>			

<u>Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate to help raise awareness of assurance practitioners about the restructured Code of Ethics</u>	<u>Whole of Year</u>	<ul style="list-style-type: none"> • <u>To hold a webinar end September 2018</u> • <u>Other speaking engagements as opportunities arise</u> • <u>Liaise with the professional bodies on joint activities to promote.</u> • <u>Journal articles</u> • <u>Set up a webpage on the revised and restructured Code</u> 	
NZAuASB Action 4.9: Promoting Understanding of the factors that Affect Audit Quality	Timing	2018/19 Planned Actions	2018/19 Actual Actions
<p><i>The focus of the NZAuASB's specific actions will be to work with other key organisations to enhance audit quality</i></p> <p>This action will comprise:</p>			

a. Actively encourage, facilitate and support other relevant organisations where appropriate to help them ensure their members understand the factors that affect audit quality, including the role of all participants in the external reporting supply chain;	Ongoing	<ul style="list-style-type: none"> Promote the audit quality framework as opportunities arise Liaise with IOD to do an awareness raising session as part of the director education series 	
b. Conducting seminars, presentations, speaking engagements and other awareness raising activities as appropriate that inform assurance users and those charged with governance about the factors that affect audit quality		<ul style="list-style-type: none"> Speaking engagements as opportunities arise XRBrief article Promote guidance developed. 	
<u>NZAuASB Action 4.10:</u> <u>Facilitating the enhancement of audit quality</u>	<u>Timing</u>	<u>2018/19 Planned Actions</u>	<u>2018/19 Actual Actions</u>
<p><i><u>The focus of the NZAuASB specific actions will be to facilitate discussions to determine if there is a need to develop a best practice guide for audit committees in New Zealand</u></i></p> <p><i><u>This action will comprise:</u></i></p>			
<u>Approaching other relevant participants in the reporting chain (for example MBIE, IoD, NZX, FMA and the audit firms) to determine if there is an appetite for the joint development of a best practice guide for audit committees in New Zealand</u>	<u>Whole of year</u>	<ul style="list-style-type: none"> <u>Arrange meetings with other relevant participants to discuss</u> <u>Determine what further action is needed</u> 	

XRB Board, NZASB and NZAuASB 2017-2018 Strategic Action Plans – Dashboard – as at 30 June 2018

Key:	
 Project completed	 Planned for a future period
 Ongoing activity	 Project deferred/delayed/not started
 Project on track / in progress	 Project/activity removed

Specific Strategies	Board Actions					
	XRB		NZASB		NZAuASB	
Maintain and enhance existing standards (Business as usual)	<ul style="list-style-type: none"> Monitoring reporting framework Supporting reporting policy work Monitoring international developments Commenting on international governance/strategy proposals <p>Amended XRB A1 to address “group” situations for Tier 4 PBEs.</p> <p>Declined request from MBIE to amend XRB A1 to address FMA exemptions.</p> <p>Regular contact with RBNZ on the need to change OICs for bank audit reports.</p> <p>Review of Appendix A of XRB A1 “When is an entity a public benefit entity” progressing.</p> <p>Active monitoring and participation in the Monitoring Group’s consultation to reform audit and ethics standard-setting including attendance at MG roundtables held in Australia.</p> <p>Submission made to Monitoring Group Consultation Paper. High level of</p>		<ul style="list-style-type: none"> Maintaining NZ standards Contributing to international due process Monitoring emerging issues <p><i>Domestic Projects:</i></p> <ul style="list-style-type: none"> Approved PBE FRS 48 <i>Service Performance Reporting</i>, Nov 2017. Developing Service Performance Reporting Guidance. Developing PBE standard based on IPSAS 40 <i>Public Sector Combinations</i>. Developing PBE standard based on IFRS 17 <i>Insurance Contracts</i>, includes establishment of PBE Insurance Working Group. Approved <i>Amendments to the Scope of FRS-42</i> 		<ul style="list-style-type: none"> Maintaining NZ standards Contributing to international due process Monitoring assurance environment <p><i>Domestic Projects:</i></p> <ul style="list-style-type: none"> Approved long association amendments to PES-1 to adopt international Code. Approved amendment to definition of PIE. Issued FAQs on auditor rotation. Auditing standard on SPI in progress. Reconsidering compelling reason amendments to PES-1 relating to independence for other assurance engagements. Preparing FAQs on rotation requirements for dual listed entities. 	

Board Actions			
Specific Strategies	XRB	NZASB	NZAuASB
	<p>mention from XRB's submission in summary commissioned by IFAC.</p> <p>Met with MBIE, MfE and Productivity Commission staff in Mar/Apr 2018 on Climate Change proposals.</p> <p>Comment letter to Productivity Commission on Climate Change draft recommendations and met with Productivity Commission on the XRB submission in Jun 2018.</p> <p>On-going dialogue with Productivity Commission.</p>	<p>(Prospective Financial Statements) May 2018.</p> <ul style="list-style-type: none"> Approved <i>RDR NZ IFRS 16 and NZ IAS 7</i>, June 2018. Approved <i>2017 Omnibus Amendments to NZ IFRS</i>, Nov 2017. Approved <i>2018 Amendments to Tier 3 and Tier 4 PBE Accounting Requirements</i>, June 2018. <p>IASB Projects:</p> <ul style="list-style-type: none"> Approved NZ IFRS 17 <i>Insurance Contracts</i>, Aug 2017. Approved NZ Equivalent to <i>IASB Conceptual Framework for Financial Reporting</i>, and <i>Updating References to Conceptual Framework in NZ IFRS</i>, May 2018. Approved NZ IFRIC 23 <i>Uncertainty over Income Tax Treatments</i>, Aug 2017. Approved 4 narrow scope amendments to NZ IFRS.¹ 	<p>IAASB Projects</p> <ul style="list-style-type: none"> ED ISA 540 (Revised) in progress <p>IESBA Projects</p> <ul style="list-style-type: none"> ED Restructured Code of Ethics in progress <p>Monitoring assurance environment:</p> <ul style="list-style-type: none"> Director Assurance Standards participating in FMA audit oversight committee meetings.

¹ *Prepayment Features with Negative Compensation* (Amendments to NZ IFRS 9), *Long term interests in Associates and Joint Ventures* (Amendments to NZ IAS 28), *Annual Improvements to NZ IFRSs 2015-2017 Cycle*, and *Plan Amendment, Curtailment or Settlement* (Amendments to NZ IAS 19).

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
			<i>IPSASB Projects</i> Comment letters issued: <ul style="list-style-type: none">• CP– <i>Financial Reporting for Heritage in the Public Sector.</i>• CP – <i>Revenue and Non-Exchange Expenses.</i>• ED 63 – Social Benefits.• ED 64 – Leases.• IPSASB Consultation Document – Proposed Strategy and Work Plan 2019–2023. Contributing to international due process: <ul style="list-style-type: none">• Conducted outreach activities. Monitoring emerging issues: <ul style="list-style-type: none">• Continued meeting of the established TRG of the NZASB on a quarterly basis.			
Maintain and enhance existing standards (Address critical issues)	Consider appropriateness of Accounting Standards Framework for incorporated societies Awaiting passing incorporated societies Act. After a temporary pause, work has now restarted on preparing these changes for Cabinet approval later in 2018.	✓	Contribute to IASB’s Disclosure Initiative Project <ul style="list-style-type: none">• Submission to the IASB on the DP.• Contributed to discussion at ASAF, IFASS and AOSSG.	✓	Develop auditing standard on auditing of service performance information Board expecting to approve limited scope review draft in July 2018.	✓

Specific Strategies	Board Actions				
	XRB	NZASB		NZAuASB	
	Expand XRB's mandate, as necessary XRB's legal mandate to issue a standard on AUP raised with MBIE. Amendment currently included Regulatory Systems Amendment Bill (which may be delayed under new Government).	✓	Promoting the discussion of Extended External Reporting Actively monitoring the IASB research into wider corporate reporting and contributing to ASAF, IFASS and AOSSG discussions on wider corporate reporting.	✓	
			Develop RDR Policy for PBE Standards Planned to commence after completion of RDR policy for for-profit accounting standards.	✓	Develop assurance standard on the examination of prospective information Commenced project.
			Improving the PBE Standards on non-exchange revenue and non-exchange expenses Issued comment letter on IPSASB's Revenue and Non-Exchange Expenses CP- IPSASB project ongoing.	✓	Develop a AUP standard. CAANZ to develop domestic AUP standard in interim due to delay in obtaining mandate. To adopt the international AUP standard once revised.
			Prepare other PBE guidance Developing service performance guidance for Tier 1 and Tier 2 PBEs.	✓	Develop guidance on use of auditing and assurance standards and relevant assurance products Base guidance developed to use as basis for more targeted guidance.
			Monitoring developments in incorporated societies financial reporting requirements Ongoing monitoring. After a temporary pause at MBIE, work has now restarted on preparing	✓	Develop a review standard on review of service performance information. To commence once auditing standard is completed.

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
			these changes for Cabinet approval later in 2018.			
			Consider amendments to standards following post-implementation review of standards frameworks. The XRB to conduct a post-implementation review of the XRB's financial reporting strategy and the New Zealand Accounting Standards Framework in the 2019–2020 period.	✓	Develop an engagement standard/guidance for smaller NFPs not required to have an audit or review. Project delayed until clarity about international developments in this area.	✓
			Post-implementation Review of Tier 3 and Tier 4 PBE Accounting Requirements Approved 2018 Omnibus Amendments to Tier 3 and Tier 4 PBE Accounting Requirements, June 2018.	✓	Developing guidance or amending NZ SRE 2410. To commence in 2 nd half of the year.	✓
					Consider whether to develop guidance for Audit Committees To commence in 2 nd half of the year.	✓
Undertake user-needs research: <ul style="list-style-type: none"> for-profit users public sector users not-for-profit users specific issues future needs 	Information needs of users of New Zealand capital market entity reports Completed. Presentation of results at various forums, including international forums.	✓	Researching information needs of Users of GPFRs See XRB comments.	✓	Assurance needs of users of non-public interest entities reports Research completed February 2018.	✓
	Information needs of users of for-profit Tier 2 entity reports Research completed, Report and Summary published in December 2017.	✓	See XRB comments.	✓	Obtaining a better understanding about the integrity of the application of ISAE (NZ) 3000 (Revised)	✓

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
	Presented findings at appropriate forums.				Completed Sept. 2017.	
	Future financial reporting/holistic reporting/ Non-financial information needs of users	✓				
	Usefulness of APMs survey completed, full report and Summary published in July 2017.					
	EER survey in conjunction with McGuinness Institute completed in Q1 2018. There was a high level of media interest following publication of the findings. McGuinness Institute has been promoting the work internationally.					
	Review of MDA requirements considered by IASB, monitor progress.					
	Information needs of rating agencies of public sector entities	✓				
Influence the international Boards: <ul style="list-style-type: none"> • IASB • IPSASB • IAASB & IESBA • NFP standard-setters 	Information needs of key NFP users	✓	Maintaining and continuing to build relationships with the IASB Visit by Sue Lloyd to Wellington and Auckland in Nov/Dec 2017. Attendance at ASAF meetings by NZASB Chair through seat shared by Australia and NZ.	✓	Building relationships -IAASB <ul style="list-style-type: none"> • Lyn Provost appointed to IAASB; Ongoing attendance by Director at IAASB meetings. • Chair and Director attended NSS meeting in May 2018. 	✓
	Undertake a post-implementation review of the standards frameworks	✓				
	IFRS governance level	✓				
	IPSASB governance level	✓				
			Contributing to IASB projects	✓	Increase the international visibility of the NZAuASB	✓

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
	IAASB/IESBA governance level Submission made to Monitoring Group on consultation to reform audit and ethics standard-setting. Active monitoring of several major disruptive influences impacting audit/assurance markets.	✓	Contributed to the discussion of the following IASB Projects at international meetings: <ul style="list-style-type: none"> Principles of Disclosure. Primary financial statements. Business Combinations under common control. 		<ul style="list-style-type: none"> Senior project manager assisted IAASB staff with ISA 540 project. Provided Chair of EER task force with SSP exposure draft and followed up by a discussion on challenges addressed. 	
	Nominate a New Zealand member on IPSASB Angela Ryan resigned due to personal circumstances, Todd Beardsworth appointed to fill casual vacancy until 31 Dec 2018. Todd nominated for a three-year period starting 1 January 2019.	✓	Maintaining and continuing to build relationships with IPSASB <ul style="list-style-type: none"> Angela Ryan reappointed Deputy Chair of IPSASB, resigned March 2018. Todd Beardsworth appointed to IPSASB Board until 31 December 2018. IPSASB Chair visited NZ in February 2018. 	✓	Supporting Lyn Provost in her role as IAASB member <ul style="list-style-type: none"> Established Technical Advisory Group and meetings on regular basis. Providing support/information to IAASB staff on various Task forces. 	✓
	NZ member appointed to IAASB NZ IAASB representative involved in various IAASB task forces and activities.	✓	Contribute to IPSASB projects Continue to support IPSASB staff in the development of various projects, which are important to NZ constituents.	✓	Building relationships - IESBA <ul style="list-style-type: none"> Senior project manager completed secondment to IESBA Dec/Jan 2018. Senior project manager attended IESBA meeting in Dec 2017. Chair and Director attended NSS meeting in May 2018. Chair and Director of IESBA to visit New Zealand in November 2018. 	✓
	Support NZ membership on international boards Ken Warren appointed to IFRS Advisory Council 2018-2020. Two New Zealand members appointed to IAASB Project Advisory Panel for EER.	✓				
	Promote the establishment of a regional public sector policy and standard setters grouping	✓	Contribute to AOSSG Working Groups	✓		

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
	<p>Raised with AOSSG delegates in Nov 2016, little interest shown, "keep it on the radar".</p> <p>Promote an international grouping of not-for-profit standard setters</p> <p>NFP working group set up under IFASS, chaired by Ian Carruthers, NZ participates in the working group.</p>	✓	<p>Member of Presentation and Disclosure, and Business Groups and Assets, Working Groups.</p> <p>Responded to various information requests and surveys.</p>			
<p>Enhance constituency engagement and support:</p> <ul style="list-style-type: none"> • Due process engagement • General engagement • Constituency education • Sectoral facilitation 	<p>Undertake general discussions with major constituent groups</p> <p>Increased activity in XRB staff presenting at appropriate fora on various topics.</p> <p>Met with MBIE, MfE and Productivity Commission staff on Climate Change proposals.</p> <p>Comment letter to Productivity Commission on Climate Change draft recommendations and met with Productivity Commission on the XRB submission.</p> <p>On-going dialogue with Productivity Commission.</p>	✓	<p>Enhance accounting standards due process consultation</p> <p>Created greater awareness of NZASB activities and due process documents issued through regular online <i>NZASB Updates</i>.</p>	✓	<p>Enhance auditing and assurance standards due process consultation</p> <ul style="list-style-type: none"> • Increased use of webinars. • One on one interviews, video conferences and teleconferences conducted with TCWG, directors, preparers and auditors on new auditor reporting. • Perspective articles in CAANZ. • Various roundtables and presentations held. 	✓
	<p>Undertake one-on-one discussions</p> <p>Regular visits by Chair and CE to principal stakeholders.</p> <p>Meetings with stakeholders as need arises on specific topics.</p>	✓	<p>Undertake on-going dialogue with major constituent groups</p> <p>The Director and Deputy Director continued to meet with key stakeholder groups in the period, in addition to Chief Executive outreach activities.</p>	✓	<p>Improve engagement relating to other assurance reports</p> <p>Maintaining database of constituency.</p>	✓

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
	Promote understanding of the new Financial Reporting Framework Key public seminar on NFP accounting held in conjunction with IPSASB Chair visit in Feb 2018.	✓	Promoting awareness of accounting standards by working with umbrella organisations <i>Regular contact with Charities Services, Treasury, OAG, and Audit NZ</i>	✓	Improve engagement with small assurance practitioners <ul style="list-style-type: none"> • <i>Maintaining database of constituency.</i> • Director presented at BDO and Staples Rodway training seminars on auditing standards. • Senior project manager presented at HLB Mann Judd Australasian Conference 	✓
	Promote importance of convergence with IASB and IAASB standards	✓	Liaising with accounting educators Visits to tertiary institutions <ul style="list-style-type: none"> • Auckland University • Otago University • Victoria University NZASB Board member from Massey University. Ongoing informal liaison with tertiary educators.	✓	Undertake on-going dialogue with auditing and assurance standards constituent groups <ul style="list-style-type: none"> • Rob Everett from FMA attended July 2017 meeting. • Board member and senior project manager presented at CAANZ audit seminar Nov 2017. • Chair participated in panel discussion on Future of Auditing at CAANZ audit conference. 	✓
	Support the functioning of the financial reporting structure through sectoral facilitation <i>A cross sectoral group for policy issues unlikely to be formed.</i>	✓	Liaising with state sector agencies <ul style="list-style-type: none"> • WG on Revenue and Non-Exchange Expenses met 	✓	Promote understanding of other assurance engagements <ul style="list-style-type: none"> • <i>Development of guidance on Compliance engagements postponed until after post implementation review.</i> 	✓

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
			<p>September, October and November 2017.</p> <ul style="list-style-type: none"> Meeting with Treasury, OAG and Audit NZ to discuss ED 64 <i>Leases</i>. 			
	<p>Promote awareness, understanding and implementation of EER</p> <p>CE working with a group of other constituents to establish a forum to promote EER in NZ.</p> <p>Roadmap for EER awareness raising and target and goals developed.</p> <p>Next steps considered by XRB at Jun 2018 meeting.</p>	✓	<p>Promoting awareness of IASB implementation support activities</p> <p>Promoted the availability of IASB's publicly available implementation support material at CA ANZ Accounting and Auditing Standards Update in five cities (October/ November 2017)</p>	✓	<p>Promote understanding of purpose of audits and reviews</p> <ul style="list-style-type: none"> Published XRBrief on Guidance for Funders on website and promoted to Charities Services and other NFPs, and via newsletter, at IAASB meetings and NSS meetings. Approved guidance for prescribers of assurance engagements, and distribution plan. Promoted on LinkedIn. Issued booklet on Small charities' assurance needs Two Articles by Chair in Law Talk about the role of the NZAuASB and trustee reporting matters. 	✓
					<p>Promote understanding of new auditor reporting requirements</p> <ul style="list-style-type: none"> Joint report with FMA on new auditor reporting published in Dec 2017 and distributed to wide audience via various media. 	✓

	Board Actions					
Specific Strategies	XRB		NZASB		NZAuASB	
					<ul style="list-style-type: none"> Issued additional FAQs on Auditor Reporting. 	
					Promote understanding of factors that affect audit quality	✓
					Promote understanding of new NOCLAR reporting requirements <ul style="list-style-type: none"> Joint perspective article with Chartered Accountants ANZ 	✓
Maintain capability within financially prudent organisation	Operating in a financially prudent manner while maintaining capability Promote continuous improvement Performance Improvement Framework self-review commenced, to be finalised in 2018. XRB stakeholder satisfaction survey completed in Jun 2018.	✓ ✓				

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 5.1
Meeting date: 5 September 2018
Subject: ED 315 Risk Assessment
Date: 24 August 2018
Prepared by: Peyman Momenan

☒ **Action Required**

☐ **For Information Purposes Only**

Agenda Item Objectives

The objective of this agenda item is for the Board to:

- Provide FEEDBACK on the issues identified in relation to the questions included in the ED ISA 315 (Revised).

Background

1. The IAASB issued the final IAASB Exposure Draft, ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement* on 16 July 2018. Comments are requested by November 2, 2018. The NZAuASB has re-issued the ED in NZ and requested comments by 8 October 2018.
2. Furthermore, on 16 of August we jointly hosted a 90-minute webinar with the Australian Auditing and Assurance Standards Board in relation to the ED. Fiona Campbell, IAASB Member and Chair of the ISA 315 Task Force explained the key revisions to the auditor's risk assessment procedures, as introduced through the recently published ISA 315 Exposure Draft.
3. The issue paper (Agenda item 5.2) includes matters we have identified in relation to the questions included in the ED. Agenda item 5.3 includes a copy of the ED document.

Next steps

4. We have arranged for two roundtable sessions (on 30 August 2018 in Wellington and on 6 September 2018 in Auckland) to receive feedback from practitioners and other stakeholders about the ED.
5. We will draft a response to the ED for the Board's consideration and approval in the October meeting, based on feedback received from the Board and from discussions in the upcoming roundtables.

Action

6. For the Board to provide FEEDBACK in relation to the ED's questions to inform the NZAuASB draft response to the ED.

Material Presented

Agenda item 5.1	Board Meeting Summary Paper
Agenda item 5.2	Issues paper.
Agenda item 5.3	IAASB ED ISA 315 (Revised)

Issues paper

1. This memo raises matters identified by staff on which we seek further feedback from the Board in order to develop a draft submission in response to the IAASB's Exposure Draft.

Overall success of the revision (Q1)

2. The IAASB has clarified that their objective in revising ISA 315 was not to change the key concepts underpinning audit risk model (as it is fundamentally sound) but to clarify and improve the identification and assessment of risk of material misstatement and to drive better risk assessments, thus enhance audit quality. The IAASB intended to achieve this overall objective by:
 - Emphasising the complexity and iterative nature of the standard
 - Improving scalability of the standard
 - Modernising and updating the ISA for an evolving business environment.
 - Better explaining how automated tools and techniques may be used in risk assessment process
 - Providing a better foundation for auditors' work around understanding an entity's use of IT in its business and system of internal controls.
 - Fostering independence of mind and professional scepticism
 - Clarifying how fraud is considered as part of the risk assessment process
3. Overall the ED has been successful in achieving the objectives. However, the level of success varies across the highlighted objectives.
 - In comparison to the extant ISA 315, the ED is a strong improvement in addressing IT and how an auditor should consider IT as part of the risk assessment process. The "Key concepts in this ISA" introductory paragraphs together with the flowcharts are also useful to help a better high-level understanding of the standard and the flow of the risk assessment. The restructure and re-arrangements of the requirements and application material is also a significant improvement over the extant ED. Introduction of the inherent risk factor is another successful addition that will be helpful to auditors in how to identify and assess inherent risk.
 - It is arguable whether scalability of the ED is an improvement over the extant ISA. (further discussed in paragraphs 5 to7)

- | |
|---|
| <ol style="list-style-type: none">4. What is the Board's view on the overall success of the ED in achieving its stated objectives? |
|---|

Scalability of the ED (Q2)

5. There is very little change in the substance of the application material included in the ED in relation to how the applicable requirements apply to small and less complex entities. The new approach adopted in the ED to include the guidance for small and less complex audits within application material paragraphs instead of under a separate heading (as in the extant

ISA) does not make a significant difference to scalability. On the other hand, the length of the ED (more than twice of the length of the extant ED) is likely to negatively affect how the standard is read and understood by SMP auditors.

6. Some of the material included to enhance scalability (including those carried forward from the extant ISA) do not appear as particularly helpful. For example, paragraph A106 states that the control environment relating to smaller and less complex entities is likely to vary from large or more complex entities. To provide an example, the ED states that if there is only a sole owner-manager running an entity, the auditor's consideration of independence of those charged with governance may not be applicable. Some further examples to explain scalability would be helpful.
7. The ED also highlights that the way the system of internal control is designed, implemented and maintained varies with an entity's size and complexity (e.g. Para A93). The ED further explains that the various aspects of the five components of the system of internal controls of smaller and less complex entities are likely to be simpler, not formally described and documented and often communicated/executed without formality. However, the ED does not address how these characteristics may make it disproportionately difficult for an auditor of a smaller and less complex entity to obtain the required understanding of the system of internal controls and document it consistent with how the system of internal controls is defined in the ED.

8. Does the Board have any comments on the scalability of the standard? Any recommendations on how scalability can be improved?
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Addressing automated tools and techniques in risk assessment (Q3)

9. Para 20 to 23 of the Explanatory Memorandum (on pages 10 and 11 of the ED) explain the adopted approach in the ED to address use of automated tools and techniques in risk assessment (sometimes referred to as Data Analytics). The provided reasoning soundly supports the adopted approach in the ED. We have not identified any areas where additional guidance is needed in relation to automated tools and techniques.

10. Does the Board have any comments on how the use of automated tools and techniques are addressed in the ED?

Enhancing the application of professional scepticism in risk assessment (Q4)

11. The way the ED intends to enhance the exercise of professional judgement is by emphasising the importance of considering contradictory evidence and information in various stages of the risk assessment. The importance of being aware of contradictory evidence may positively impact professional scepticism. However, its impact is likely to be limited as professional scepticism is likely to be more strongly associated with the auditors' characteristics (e.g. scepticism trait, knowledge, personality type etc) and the audit environment (audit firm culture, client relationships, incentives and accountability arrangements) than with definitions in the auditing standards.
12. Another way the ED intends to enhance professional scepticism is including the addition that the objective of risk assessment procedures is to obtain sufficient appropriate audit evidence. This matter is separately considered under paragraphs 22 to 25 below.

13. Does the Board have any comments on whether the ED will be helpful in enhancing professional scepticism?

Clarity of the purpose of obtaining an understanding of the entity's system of internal controls (Q5a)

14. We support the IAASB's conclusion that obtaining an understanding of the system of internal controls is a fundamental part of the auditor's risk assessment. Paragraphs A15, A47, and A200 all provide a reasonable explanation why understanding the system of internal controls is required in an audit even if there is no expectation of reliance on internal controls (i.e. control risk defaulted to maximum). However, this is not clearly explained in paragraph 4. The ED could be clearer in emphasising the inherent risk component of obtaining an understanding of the internal control system by changing the second sentence in paragraph 4 as follows:

The identification of **preliminary** risks of material misstatement at the assertion level is performed before consideration of any controls.

The above change makes it clearer that understanding the system of internal control is relevant to auditor's identification and assessment of inherent risk as well as control risk.

15. What is the Board's view on the clarification of the purpose understanding the entity's system of internal controls?

Clarity of what controls are relevant to the audit(Q5b)

16. The ED's approach to create a consolidated list of controls that the IAASB is of the view are always relevant to audit (included in paragraphs 39 to 41 of the ED) is very helpful and clarifies what controls are relevant to the audit. As paragraph 37 of the explanatory memorandum explains these relevant controls are likely to be "direct controls". We support the IAASB's conclusion that the auditor may identify controls in the control environment, the entity's risk assessment process or the entity's process to monitor controls that are also relevant to the audit. However, it may be helpful to provide some examples to better demonstrate this point (e.g. in para A104)

17. What is the Board's view on whether the identification of controls relevant to the audit have been enhanced and clarified in the ED?

New IT-related concepts and definitions

18. The ED is a substantial improvement over the extant ISA in relation to how information technology underpinning an entity's system of internal controls is relevant to audit. This includes:

- Clarifying how IT may relate to each component of internal controls.
- The introduction of the four criteria (included in paragraph 40 of the ED) as what IT controls are relevant to audit.
- Providing a foundation for the auditor's understanding of the entity's use of information technology and what may result in risks arising from the entity use of IT.

- Appendix 4 of the ED which provides further consideration related to general IT controls.

19. We further support the ED's approach of addressing risks arising from using IT by contrasting an entity with a very basic and simple IT environment to an entity using multiple sophisticated IT applications relevant to its financial reporting objectives. The ED further explains that where an entity's use of IT applications relevant to its financial reporting is limited to use of commercial, reputable software (e.g. using an accounting software) and that the auditor does not intend to rely on the controls within the software (e.g. undertake substantive procedures to test reports and information produced by the entity) the auditor may conclude that there are no IT applications relevant to audit (paragraphs A 149 and A181). We however believe that even in such circumstances, there is still a need for the auditor to obtain an understanding of the entity's general IT controls that underpin the software. E.g. obtaining an understanding of the general IT controls discussed in paragraph 2 (a) of Appendix 4 to the ED are likely to be important to an audit that only uses a simple, commercial accounting software.

20. What is the Board's view on how the ED addresses the entity's use of IT and what aspects of it are relevant to audit?

Purpose of performing risk assessment procedures

21. The IAASB has clarified that the purpose of performing risk assessment procedures is to obtain sufficient, appropriate audit evidence as the basis for the identification and assessment of the risks of material misstatement. (Paragraph 17 ED ISA 315)
22. The definition of audit evidence is "Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information."
23. The term audit evidence seems to be out of place in the requirement in paragraph 17. Usually the auditor collects audit evidence to support the conclusion (i.e. evidence to support that the risk has been reduced, rather than as evidence that the risk is there).
24. We believe that the intention is to create a more robust basis for the risk assessment however consider that the term "audit evidence" is too strong in this instance and is contrary to the definition of audit evidence. We suggest deleting the words as indicated "The auditor shall design and perform risk assessment procedures to obtain an understanding of:
- The entity and its environment
 - The applicable financial reporting framework
 - The entity's system of internal control

~~To obtain sufficient appropriate audit evidence as the basis for the identification and assessment of the risks of material misstatement at the financial statement and assertion levels. Risk assessment procedures by themselves, however, do not provide sufficient appropriate audit evidence on which to base the audit opinion.~~

25. What is the Board's view on the clarification of the purpose of the risk assessment procedures?

Separate assessments of inherent risk and control risk (Q6a)

- 26. A key change proposed by ED ISA 315 is to require a separate assessment of inherent and control risk at the assertion level (refer to paragraphs 45-50 and A201-A235 of the ED).
- 27. Separate assessments of inherent and control risk were introduced in the ISA 540 project and will have conforming amendments to ISA 200.
- 28. ISA 330 requires the auditor to consider inherent risk and control risk separately in order to respond appropriately to assessed risks of material misstatement (ROMM).
- 29. We support the separate assessment and consider the proposed requirements and application material to be appropriate.
- 30. The ED also makes it explicit that the auditor assesses control risk as maximum if not testing operating controls.

31. Does the Board have any additional comments and comments on the requirements in paragraph 45-50 and A201-A235?

Inherent risk factors (Q6b)

- 32. ED ISA 315 proposes to define "inherent risk factors (IRF)" as "Characteristics of events or conditions that affect susceptibility to misstatement of an assertion about a class of transactions, account balance or disclosure, before consideration of controls. Such factors may be qualitative or quantitative, and include complexity, subjectivity, change, uncertainty or susceptibility to misstatement due to management bias or fraud."
- 33. We consider emphasising factors including complexity, subjectivity, change, uncertainty or susceptibility to misstatement due to management bias or fraud is helpful and will drive more consistency as to the types of and reasons for identification of risks. We have not identified any additional factors.
- 34. However, the proposed definition includes the words "may be qualitative or quantitative". It is unclear how the words "qualitative or quantitative" relate to the susceptibility to misstatement and we wonder if these words are superfluous in the definition?
- 35. The application material (paragraph A5) lists the above-mentioned factors as qualitative inherent factors. Paragraph A6 describes other risk factors that include the quantitative or qualitative significance of the class of transaction, account balance or disclosure.
- 36. An implication may be that low risk large items (quantitatively large) are identified. Just because a balance is large however does not equate to a high risk of ROMM? Similarly, a low balance may have a high risk of understatement.
- 37. We would suggest deleting the words that have been underlined in the proposed definition above as well as in paragraph A5. The reference to qualitative and quantitative makes most sense as it is used in the first bullet point of paragraph A6. Alternatively, we suggest more examples to explain why these words are relevant to the definition of an IRF, i.e. why the size of a balance impacts on the susceptibility to misstatement.

38. **Does the Board have any comments on the definition of and application material related to IRFs? Does the Board agree with the reference to “quantitative and qualitative” in the definition of IRFs?**

Spectrum of inherent risk (Q6c)

39. ED ISA 315 has introduced the idea of a “spectrum of inherent risk” in introductory paragraph 5 and application material (paragraphs A224) to drive consistency in the identification and assessment on ROMM. The idea recognises that IRFs individually or in combination increase inherent risk to varying degrees to provide a frame of reference. This concept is included in the definition of significant risk. There is still a requirement to separately determine significant risks because of the focused work effort in other ISAs on these types of risks.
40. We support the introduction of the concept. Acknowledging the spectrum of risk is a practical way to identify and then assess inherent risk.
41. The concepts of likelihood of occurrence and magnitude of possible misstatement are also useful, i.e. in planning the audit effort the auditor will take both of these into account.

42. **Does the Board have any comments on the concept of spectrum of inherent risks?**

Significant classes of transactions, account balances and disclosures and relevant assertions (Q6d)

43. ED ISA 315 introduces a new definition of significant classes of transactions, account balances and disclosures as “a class of transactions, account balance or disclosure for which there is one or more relevant assertion”.
44. We agree that defining significant classes of transactions, account balances and disclosures is useful and may help to clarify the scope of the auditor’s understanding of the information system and the scope for the auditor’s responses to the assessed ROMM.
45. A relevant assertion is defined as “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”.
46. The IAASB’s deliberations highlighted the need to explain the level of likelihood that should be taken into account. “Reasonable possibility” is similar to a term used by the US Public Company Accounting Oversight Board (PCAOB). The definition explains that this term equates to “more than remote”.
47. The FASB Standards use the following scale:
- Probable – the chance of the future event is likely
 - Reasonably possible – the chance of the future event is more than remote but less than likely
 - Remote – the chance of the future event is slight.

48. Paragraph A211 refers to where there is a remote possibility with respect to an assertion, there are no ROMMs and the assertion is not relevant.
49. Without the context of the FASB standards, we consider that the current drafting could be clarified further as there seems to be a difference between reasonably possible and more than remote, which may be confusing as currently drafted. More guidance as to how the auditor should assess the probability and evidence this judgement would be useful.

50. Does the Board have any comments on the references to both reasonable possibility and likelihood that is more than remote?

51. The requirement to determine relevant assertions is in paragraph 46 of the ED and additional application material is in paragraphs A211-A214.

52. Does the Board have any views as to whether there is sufficient guidance to explain how a relevant assertion is determined and how they assist in identifying ROMMs?

Significant risks (Q6e)

53. The IAASB is proposing to amend the definition of significant risk as “an identified risk of material misstatement:
- For which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which one or a combination of the inherent risk factors affect the likelihood of a misstatement occurring OR the magnitude of potential misstatement should that misstatement occur: or
 - That is to be treated as a significant risk in accordance with the requirements of other ISAs.”
54. The IAASB is responding to inspection findings highlighting inconsistency in the way in which significant risks are determined. The extant standard defines a significant risk as “an identified and assessed risk of material misstatement that, in the auditor’s judgement, requires special audit consideration”. The extant definition has a focus on the auditor’s response to the risk rather than the nature of the risk. The idea is to focus on risks that are on the upper end of the spectrum of inherent risk, and implies that there may be one or more risks that could be determined to be significant.
55. The use of the word “OR” has been highlighted in this paper and was purposefully included (as opposed to AND).
56. We consider that this is a significant difference to the extant standard and potentially significantly broadens the number of significant risks.
57. We support a focus on the nature of the risk rather than then response to the risk but consider that auditors would best focus on risks for which there is a high likelihood AND high magnitude. (i.e. using AND rather than OR will highlight those risks that are at the higher spectrum of risk).
58. This proposal would require the auditor to focus on risks that may have a high magnitude but a low likelihood and also on risks that have a high likelihood but a low magnitude. We do not agree that all of these risks would necessarily achieve the objective of the upper end

of the spectrum of risk, rather would broaden the identification of significant risks much further along than at the “upper end” of the spectrum.

- 59. We wonder what value is added by the auditor spending significant audit effort on risks that are most unlikely to occur?
- 60. We also wonder if there is value added by the auditor spending significant audit effort on risks that have a high likelihood but a very low impact in terms of magnitude?
- 61. We would recommend that the IAASB change the word OR to AND to achieve the objective described.
- 62. A key challenge we see for auditors will be to evidence the likelihood of something occurring. Another argument is whether it is the role of the auditor to be able to assess the likelihood of something occurring (E.g. how would the auditor assess and evidence the likelihood of another big earthquake in Christchurch, or the likelihood of Mycoplasma bovis being contained or how far it will spread?)

63. Does the Board agree with the revised definition of a significant risk? Do you consider that the word “AND” would achieve what the IAASB is trying to achieve?

ROMM at the financial statement level (Q7)

- 64. ED ISA 315 separates the identification of ROMM and the assessment of ROMM as two discrete steps (Refer to para 45-48)
- 65. The IAASB has added additional guidance in relation to the auditor’s assessment of ROMM 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. (Refer to paragraph 47 and A 215-A220 of the ED).
- 66. This explains that ROMM at the financial statement level may be pervasive (i.e. not possible to identify the specific assertions, or many assertions are identified.)
- 67. Paragraph A216 and A218 cross reference to requirements. Although this is already included in the ED it is useful to have these connections made in the application material.
- 68. We consider that this additional guidance is useful.

69. Does the Board have any comments on the additional application material in relation to the assessment of ROMM at the financial statement level?

Stand-back requirement (Q8)

- 70. The IAASB is proposing to add a new stand-back provision (paragraph 52 of the ED) to capture classes of transactions, account balances and disclosures that are not significant, but which are material. I.e. it requires the auditor to identify any classes of transactions, account balances and disclosures that are quantitatively or qualitatively material that have not been identified as significant and evaluate whether the conclusion that there are no relevant assertions remains appropriate.
- 71. Currently, ISA 330 *The Auditor’s Response to Assessed Risk* includes a requirement in paragraph 18 for the auditor to design and perform substantive procedures for each material class of transactions, account balance and disclosure. The ED proposes to make

conforming amendments to ISA 330 to refer to quantitatively or qualitatively material consistent with paragraph 52 of ED ISA 315.

72. We consider that the addition of a stand-back requirement is useful and will promote a more robust framework to ensure that all relevant assertions are addressed in the audit.
73. We do not consider that paragraph 18 of ISA 330 is needed if this stand-back requirement is introduced. If there are no relevant assertions, why would the auditor need to perform any audit procedures?
74. An example of the type of item that may fall into this category may be when the auditor does not identify Property, Plant and Equipment as a significant balance, but it may be material due to the value of land held. The stand-back requirement would ensure that the auditor considers the assertions related Property, plant and equipment (i.e. the ownership of the land may be a key assertion – i.e. there may remain a need for the auditor to confirm that the title of the land remains with the entity.)
75. We consider that this would be met by the stand-back requirement and therefore it is not necessary to include this in both ISA 315 and ISA 330.

76. What is the Board's view on the proposed stand-back requirement, proposed conforming amendments to ISA 330 and the ongoing need for paragraph 18 in ISA 330 if the stand-back requirement is introduced?

Conforming and Consequential amendments (Q9)

77. We will raise any matters identified with respect to the conforming and consequential amendments at the October meeting when preparing a draft submission for consideration.

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 6.1

Meeting date: 5 September 2018

Subject: ED 540 Estimates

Date: 13 August 2018

Prepared by: Sharon Walker

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Agenda Item Objectives

The objective of this agenda item is for the Board to:

- NOTE the final ISA 540 (Revised) and related conforming and consequential amendments (currently waiting on Public Interest Oversight Board approval)
- AGREE with our recommendation that there are no compelling reason amendments needed to ISA 540 (Revised) when adopting for use in New Zealand.

Background

International Process

1. The IAASB consultations in developing its Strategy for 2015-2019¹ and related Work Plan for 2015-2016² indicated a need for the International Auditing and Assurance Standards Board (IAASB) to take action to address issues relevant to the application of ISA 540³ in audits of financial institutions, as well as more broadly.
2. Since early 2015, the IAASB has undertaken outreach activities to identify issues regarding the auditing of accounting estimates for financial institutions and other entities. The outreach indicated that regulators and auditors of financial institutions were of the view that the IAASB should focus on the issues for audits of financial institutions arising from IFRS 9⁴, ahead of its effective date for financial statements for annual periods beginning on or after 1 January 2018. IFRS 9 adopts expected credit loss models for loan loss provisions, which fundamentally changes the way that banks and other entities account for their loan assets and other credit exposures.

¹ http://www.ifac.org/system/files/publications/files/IAASB-Strategy-2015-2019_0.pdf

² <http://www.ifac.org/system/files/publications/files/IAASB-Work-Plan-2015-2016.pdf>

³ International Standard on Auditing (ISA) 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*

⁴ IFRS 9, *Financial Instruments*

3. After listening to key stakeholders, the IAASB concluded that most, if not all, of the issues identified with respect to expected credit losses would be equally relevant when auditor other complex accounting estimates. Accordingly, the IAASB concluded that a holistic revision of ISA 540 should be undertaken.
4. The IAASB issued for public comments its exposure draft (ED) of proposed ISA 540 (Revised), *Auditing Accounting Estimates, including Related Disclosures*, in April 2017 with comments due on 1 August 2017.
5. The ED required auditors to sharpen their focus on risks of material misstatements arising from accounting estimates, and to address those risks with more granular audit requirements. Specifically, the ED:
 - Enhanced requirements for risk assessment procedures to include specific facts related to accounting estimates, namely complexity, judgement, and estimation uncertainty;
 - Set a more detailed expectation for the auditor's response to identified risks, including augmenting the auditor's application of professional scepticism; and
 - Was scalable regardless of the size or sector of the business or audit firm.
6. Sixty-nine comment letters were received by the IAASB on its ED, including submissions from the majority of the monitoring group members. While there was much support for the IAASB's objectives in revising ISA 540, respondents raised several significant concerns with the proposals including:
 - Clarity/readability/operability of the proposed standard; complex wording and sentence structure, volume of application material.
 - Connectivity of proposed ISA 540 to other standards, for example, ISA 315 (Revised), ISA 330 and ISA 500 can be enhanced.
 - Focus on complex accounting estimates, e.g., IFRS 9. Proposed ISA 540 is too complicated for simple accounting estimates.
 - Support for risk factors (complexity, judgement and estimation uncertainty) but concerns about how they are applied in the risk assessment process and response; the effect of interrelationships between the factors; structuring the work effort by risk factor is overly complex and may consequently result in inconsistencies, repetition and inefficiencies.
 - Perceived difficulties with operationalising the low inherent risk threshold.
 - Overly prescriptive nature of the risk assessment procedures for simple accounting estimates.
 - Use of point estimates and ranges – when management does not adequately address estimation uncertainty, the auditor should not be responsible for developing a range; more guidance is needed when the range is multiples of materiality.
7. The IAASB discussed significant comments and related task force proposals at its September, October and December 2017 and January (conference call), March, April (conference call) and June 2018 meetings.
8. Key matters raised in the NZAuASB submission and how those matters were addressed are covered in Appendix 1 of this paper. A copy of the submission is available on the [XRB website](#).

9. In response to the comments received from all respondents, the following significant amendments to the ED and related conforming amendments were made:
- Removed the threshold of low/not low. Reinforced scalability by reinforcing the existing concept of the spectrum of risk and drawing upon the existing material in ISA 315 (Revised) and ISA 330.
 - Aligned the terms used for the risk factors with those of the U.S. Public Company Accounting Oversight Board's proposals – estimation uncertainty, complexity, subjectivity.
 - Revised the structure of the standard, basing the work effort requirements around the testing strategies and methods, data and assumptions.
 - Gave more prominence to estimation uncertainty in identifying and assessing the risks of material misstatement.
 - Enhanced significantly the introductory material, including key concepts and the description of the spectrum of risk.
 - Removed superfluous and gratuitous application material.
10. The IAASB also amended the effective date from that proposed in the ED. It concluded that an effective date for periods beginning on or after 15 December 2019 would be more appropriate given that ISA 540 (Revised) affects the planning and risk assessment activities for an audit; firms need time to update their methodologies and audit tools, develop training materials and train staff; smaller firms rely on external providers; and some national standard setters need time to translate the standard and develop supplemental implementation material and in some cases expose the standard before it will be effective in their jurisdiction. Early implementation is permitted.
11. In June 2018, the IAASB approved for issue, subject to approval by the Public Interest Oversight Board (PIOB) that due process has been followed, ISA 540 (Revised) and related conforming amendments. The revised ISA will be effective for audits of financial reporting periods beginning on or after 15 December 2019. The final standard, subject to PIOB approval, is anticipated in October 2018.
12. The IAASB determined that the changes to the ED did not meet the requirements for re-exposure.

Domestic Process

13. The NZAuASB sought feedback from constituents on the IAASB's ED through round table discussions held on May 30 in Auckland and June 1 in Wellington. Participants at the combined round table discussions represented the following: OAG, CAANZ, FMA, PWC, EY, Grant Thornton, and AUT. A formal submission was also received from the OAG.
14. The NZAuASB's submission to the IAASB was prepared based on feedback received from the round table discussions, the Board at its June 2017 meeting, and from a submission received.
15. No compelling reason amendments were identified by respondents. Extant ISA (NZ) 540 contains no compelling reason amendments.

Australia

16. The AUASB approved the issue of Exposure Draft ASA 540 *Auditing Accounting Estimates and Related Disclosures* and related conforming amendments at its 31 July 2018 meeting held via teleconference.
17. One of the key issues that the AUASB has centres around the expectation of the auditor in relation to the point estimate/range calculation. Some AUASB members are concerned about the shift of onus from preparer to auditor where the preparer has not fully understood or taken into account estimation uncertainty. To this end, the AUASB is seeking feedback on these particular requirements in its invitation to comment.
18. The AUASB has not identified any compelling reason amendments at this stage.

Matters for Consideration

19. Appendix 1 to this paper includes a table showing how the IAASB has addressed comments the NZAuASB raised in its submission. The IAASB draft Basis of Conclusion is available at agenda item 6.2.
20. In our view there are no compelling reason amendments to address when adopting the ISA 540 (Revised) in New Zealand, subject to any compelling reason amendments that may be identified by the AUASB as a result of the exposure process in Australia.
21. The Board is asked to:
 - NOTE the final ISA 540 (Revised) and related conforming and consequential amendments,
 - AGREE with our recommendation that there are no compelling reason amendments needed to ISA 540 (Revised) when adopting for use in New Zealand.

Next steps

22. We intend to present the Board with the proposed ISA (NZ) 540 (Revised) at the October meeting for APPROVAL.

Material Presented

Agenda item 6.1	Board meeting summary paper
Agenda item 6.2	IAASB Draft Basis of Conclusions (Non-public Document)
Agenda item 6.3	ISA 540 (Revised) – clean
Agenda item 6.4	Conforming and consequential amendments

Appendix 1 – Disposition of comments, NZAuASB submission to IAASB

The NZAuASB's submission expressed the following key concerns:

<p>Q1 Has ED-540 been appropriately updated to deal with evolving financial reporting frameworks as they relate to accounting estimates?</p> <p>Concern that the focus of ED-540 is heavily weighted towards complex accounting estimates found in the banking and insurance industries and recommends that additional examples could be included in the guidance that reflect auditing issues relating to accounting estimates that are common in other sectors.</p> <p>ED-540 does not adequately address auditing issues relating to accounting estimates in the public sector.</p>	<p>Concern addressed. ISA 540 has been significantly redrafted in a much more neutral tone.</p>
<p>Q2 Do the requirements and application material of ED-540 appropriately reinforce the application of professional scepticism when auditing accounting estimates?</p> <p>Concern that the level of granularity in the requirements of ED-540, in particular paragraphs 17-19, may create a compliance mentality, rather than reinforce the notion of professional scepticism when auditing accounting estimates</p> <p>While the auditor does consider complexity, use of judgement and estimation uncertainty when auditing accounting estimates, each factor is not separately considered as appears in the case in ED-540. Rather, the factors are integrated and often overlap.</p> <p>Supportive of including a stand-back provision in ED-540, but the stand-back provision should be incremental to the requirement in ISA 330. Recommend that the requirement in paragraph 22 of ED-540 focus on the auditor's consideration of management bias and the auditor's evaluation of management's decisions relating to the accounting estimates. The requirements to evaluate whether the assessments of the risk of material misstatement at the assertion level remain appropriate and whether sufficient appropriate audit evidence has been obtained (as drafted in paragraphs 22(a) and 22(b)) are already sufficiently addressed in ISA 330.</p>	<p>Concern addressed.</p> <p>Complexity, use of judgement and estimation uncertainty are no longer treated as separate requirements. The ISA recognises that estimation uncertainty is inherent in all estimates. The auditor is required to take into account the degree to which the accounting estimate is subject to estimation uncertainty and the degree to which it is affected by complexity, subjectivity or other inherent risk factors (para 16)</p> <p>Minimal changes to the stand-back provision. It now applies to all estimates rather than only those that are subject to the risk factors, estimation uncertainty, complexity, management judgement.</p>

<p>The stand-back provision should apply to the auditor's initial assessment of inherent risk for all accounting estimates, not just those that are initially identified as being "not low" risk.</p>	
<p>Q3 Is ED-540 sufficiently scalable with respect to auditing accounting estimates, including when there is low inherent risk?</p> <p>ED-540 is not sufficiently scalable with respect to auditing accounting estimates.</p> <p>Concern with the requirement to assess risk of material misstatement related to accounting estimates as "low" or "not low" based on inherent risk. The concepts of "low" and "not low" have not been clearly defined and there is a disconnect with the assessment of risk based on the extant standards. Based on the examples provided in paragraph A72 only the simplest of accounting estimates will be assessed with inherent risk of "low".</p> <p>For those accounting estimates for which the inherent risk is assessed as "not low" there is a broad range of different types of estimates, some of which will have a higher inherent risk than others. There is no category of inherent risk between "low" and "not low". The granular requirements in paragraphs 17-19, however, apply to all estimates regardless of the level of inherent risk above "not low". The drafting of these requirements at such a granular level may reduce the application of professional judgement of the auditor and result in a compliance based approach to auditing the estimate.</p>	<p>Concern addressed.</p> <p>The consideration of inherent risk as low risk/not low risk has been removed. Rather the "spectrum of inherent risk" is explained in the key concepts section of ISA 540 (Revised).</p> <p>Application material is enhanced to explain relationship between risk assessment and responses to the risk of material misstatement (further audit procedures).</p> <p>Granularity of requirements has been reduced.</p>
<p>Q4 When inherent risk is not low (see paragraphs 13, 15 and 17-20)</p> <p>(a) Will these requirements support more effective identification and assessment of, and responses to, risks of material misstatement (including significant risks) relating to accounting estimates, together with the relevant requirements in ISA 315 (Revised) and ISA 330?</p> <p><i>Objectives-based vs rules-based requirements</i></p> <p>Paragraphs 17-19 are not sufficiently objectives-based. There is not sufficient flexibility within the requirements, and as drafted, these requirements,</p>	<p>Concern addressed</p> <p>Risks are no longer assessed as low/not low.</p> <p>The consideration of the risk factors (estimation uncertainty, complexity, subjectivity) have been incorporated into the identification and assessment of the risks of material misstatement. (paragraphs 16-17).</p> <p>For all estimates, the auditor's response to assessed risks includes one or more of:</p> <ul style="list-style-type: none"> • Obtaining audit evidence from events occurring up to the date of the auditor's report

<p>due to their granularity, will drive a compliance mentality rather than auditors using their judgement in addressing the specific risks resulting from each of the factors.</p> <p>As drafted, the requirements apply to all estimates with an inherent risk assessed as “not low”. The auditor uses judgement to determine the extent of work effort required. In our view, the requirement is that the auditor obtain sufficient appropriate audit evidence. The matters under paragraphs 17-19 that the auditor is required to obtain sufficient appropriate audit evidence about are in our view application material to the requirement. For example, in paragraph 17, an objectives-based requirement would be that the auditor obtain sufficient appropriate audit evidence related to management’s use of a complex method (including complex modelling) or when management’s method otherwise involves the use of specialised skills or knowledge. The matters indicated in paragraphs (a) – (e) are the matters that auditor may consider in obtaining sufficient appropriate audit evidence.</p>	<ul style="list-style-type: none"> • Testing how management made the accounting estimate • Developing an auditor’s point estimate. <p>The auditor tests controls when the auditor intends to rely on controls or when substantive procedures alone cannot provide sufficient audit evidence (control testing was previously included as a required response).</p>
<p><i>Developing an auditor’s point estimate or range</i></p> <p>Paragraph 19(b) of ED-540 requires the auditor, to the extent possible, to develop an auditor’s point estimate or range when management has not appropriately understood and addressed estimation uncertainty. It is generally not common practice for the auditor to develop a range. Rather, the auditor evaluates the models, data and assumptions used by management in determining their point estimate as required by extant ISA 540. Extant ISA 540 allows the auditor to determine the appropriate further audit procedures in responding to the assessed risk of material misstatement.</p> <p>The approach taken in ED-540, requiring the auditor to develop a point estimate or range, may be seen as confrontational, pitting the auditor against the preparer. In addition, ED-540 assumes a certain level of preparer sophistication. In the SME/SMP environment, in particular, the preparer may not have the sophistication necessary to understand and address estimation uncertainty. When this is the case, the requirement for the auditor to develop a point estimate or range may present an independence issue, resulting in the risk that the auditor is auditing his or her own work.</p> <p>When, in the auditor’s judgement, management</p>	<p>Concerns addressed.</p> <p>Revised paragraph 27 addresses when management has not taken appropriate steps to understand or address estimation uncertainty. Management is first requested to perform additional procedures to understand estimation uncertainty (as suggested in the NZAuASB submission). If the auditor determines that management’s response to the auditor’s request is not sufficient, to the extent practicable, the auditor is required to develop a point estimate or range. In addition, the auditor is required to evaluate whether a deficiency in internal control exists, and if so, communicate appropriately.</p>

<p>has not properly understood and addressed estimation uncertainty, the auditor firstly needs to request that management consider alternative assumptions or provide additional disclosures. If management is unable or refuses to do so, the auditor should then be required to consider the possibility of developing an auditor's point estimate or range. If the auditor is unable to develop a point estimate or range, then the auditor needs to consider the impact on the audit and the auditor's opinion.</p>	
<p>(b) Do you support the requirement in ED-540 for the auditor to take into account the extent to which the accounting estimate is subject to, or affected by, one or more relevant factors, including complexity, the need for the use of judgment by management and the potential for management bias, and estimation uncertainty?</p> <p>Supportive of the requirements in ED-540 for the auditor to take into account the extent to which the accounting estimate is subject to, or affected by, complexity, the need for the use of judgement, including the potential for management bias, and estimation uncertainty. Feedback from practitioners indicates that these factors are generally already being considered. Often these factors are integrated and overlap. In practice each factor is not necessarily considered discretely as appears contemplated by ED-540. Rather, the auditor may design and perform procedures that do not compartmentalise the factors in this way.</p> <p>Concerns about the prescriptive nature of the requirements in paragraphs 17-19 to address these factors (refer 4a)</p>	<p>Concerns addressed.</p> <p>Consideration of the risk factors is now included in the identification and assessment of the risk of material misstatement. ISA 540 does not require separate consideration of estimation uncertainty, complexity and subjectivity.</p>
<p>(c) Is there sufficient guidance in relation to the proposed objectives-based requirements in paragraphs 17-19 of ED-540? If not, what additional guidance should be included?</p> <p>As noted in the introductory comments, there are a number of sections within ED-540 that contain unnecessary content. Either because they:</p> <ul style="list-style-type: none"> • state the obvious; • discuss fundamental concepts which should be well understood by the auditor and are not specific to auditing accounting 	<p>Concerns addressed.</p> <p>Application material has been considerably reduced.</p>

<p>estimates; or</p> <ul style="list-style-type: none"> • repeat issues already addressed in the exposure draft. <p>This has the effect of making the standard longer than it needs to be (ED-540 includes 17 requirements and 211 application paragraphs).</p> <p>Recommend that the IAASB carefully consider the relevance of each of the 211 application paragraphs to ED-540 with a view to determining whether the guidance is essential.</p>	
<p>Q5 Does the requirement in paragraph 20 (and related application material in paragraphs A128-A134) appropriately establish how the auditor's range should be developed? Will this approach be more effective than the approach of "narrowing the range", as in extant ISA 540, in evaluating whether management's point estimate is reasonable or misstated?</p> <p>As noted previously, it is not common for the auditor to develop a range. From a practical perspective, we see very little difference in the proposals in ED-540 compared with extant ISA 540.</p> <p>Paragraph A134 indicates that an auditor's range for an accounting estimate may be multiples of materiality and that in such circumstances, the auditor's evaluation of the reasonableness of the disclosures about estimation uncertainty becomes increasingly more important. Additional application material to address the auditor's considerations when this is the case would be helpful.</p>	<p>Additional guidance has been included. See paragraph A125. This is likely to be an area that will continue to create challenges in practice due to its subjective nature.</p>
<p>Q6. Will the requirement in paragraph 23 and related application material (see paragraphs A2-A3 and A142-A146) result in more consistent determination of a misstatement, including when the auditor uses an auditor's range to evaluate management's point estimate?</p> <p>Consistent determination of misstatements will continue to present a challenge, particularly for those misstatements that represent judgemental misstatements rather than factual misstatements. In relation to determining misstatements, ED-540 does not provide sufficient guidance on the auditor's assessment and evaluation of misstatements that arise as a result of a difference in judgement. Guidance that addresses the auditor's considerations in relation to judgemental</p>	<p>Very little change to the ED. The auditor will need to look to ISA 450 for guidance in evaluating misstatements, including misstatements of estimates.</p> <p>Guidance around consideration of disclosures continues to be spread throughout the ISA.</p>

<p>misstatements would be helpful, for example, the auditor's considerations when determining whether to request management to adjust for a judgemental misstatement.</p> <p>The requirement in paragraph 23 applies to disclosures as well as amounts recorded in the financial statements. However, applicable application material appears to be scattered throughout ED-540. For example, paragraphs A124-A125 discuss what the auditor may do when the auditor concludes that disclosure of estimation uncertainty is not reasonable in light of the circumstances and facts involved. This guidance would be more appropriately included in the discussion of misstatements. Similarly, paragraphs A135-A138 address disclosures related to accounting estimates. A robust discussion (within one section rather than in separate sections in the application material) of the auditor's considerations when determining the reasonableness of disclosures (in addition to those relating to estimation uncertainty) would significantly enhance the standard and lead to more consistent determination of misstatements related to disclosures</p>	
<p>Q7 With respect to the proposed conforming and consequential amendments to ISA 500 regarding external information sources, will the revision to the requirement in paragraph 7 and the related new additional application material result in more appropriate and consistent evaluations of the relevance and reliability of information from external information sources?</p> <p>Supportive of the inclusion of the proposed conforming and consequential amendments to ISA 500 with respect to external information sources.</p>	<p>ISA 200 is amended to explain that a separate assessment of inherent risk and control risk is required by ISA 540 (Revised).</p> <p>No other significant changes to the conforming amendments in finalising the ISA.</p>
<p>Q8</p> <p>(a) Translations</p> <p>(b) Effective Date</p> <p>No comment on potential translation issues.</p> <p>Support an effective date of approximately 18 months after approval of the final ISA with early application permitted and encouraged.</p>	<p>Effective date delayed to periods beginning 15 December 2019</p>

<p>General Comments</p> <p>The flowchart supplement to ED-540 was very helpful in explaining the overall approach of the standard. Recommend the IAASB consider incorporating such a flowchart in the introductory material to the standard</p>	<p>Several respondents commented that the flow chart was helpful, however, this has not been included in the final ISA.</p> <p>Not necessary considering the changes made in finalising ISA 540 (Revised).</p>
<p>Definition of the terms significant assumptions and significant data would be helpful. The current description in A35 is lost in the myriad of application material.</p>	<p>Minor comment, no change.</p>
<p>Paragraph A1, consider adding the following additional examples as suggested by practitioners:</p> <ul style="list-style-type: none"> • Biological assets • Investment properties 	<p>Minor comment, no change</p>

Agenda Item 2-C Updated IAASB Approved Text

ISA 540 (Revised) – IAASB Approved Text

Note to Readers: This is the final text of ISA 540 (Revised), which was approved by the IAASB in June 2018. The public release of the ISA is subject to the approval of the due process by the Public Interest Oversight Board in September 2018.

INTERNATIONAL STANDARD ON AUDITING 540 (REVISED) AUDITING ACCOUNTING ESTIMATES AND RELATED DISCLOSURES

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements. Specifically, it includes requirements and guidance that refer to, or expand on, how ISA 315 (Revised),¹ ISA 330,² ISA 450,³ ISA 500⁴ and other relevant ISAs are to be applied in relation to accounting estimates and related disclosures. It also includes requirements and guidance on the evaluation of misstatements of accounting estimates and related disclosures, and indicators of possible management bias.

Nature of Accounting Estimates

2. Accounting estimates vary widely in nature and are required to be made by management when the monetary amounts cannot be directly observed. The measurement of these monetary amounts is subject to estimation uncertainty, which reflects inherent limitations in knowledge or data. These limitations give rise to inherent subjectivity and variation in the measurement outcomes. The process of making accounting estimates involves selecting and applying a method using assumptions and data, which requires judgment by management and can give rise to complexity in measurement. The effects of complexity, subjectivity or other inherent risk factors on the measurement of these monetary amounts affects their susceptibility to misstatement. (Ref: Para. A1–A6, Appendix 1)
3. Although this ISA applies to all accounting estimates, the degree to which an accounting estimate is subject to estimation uncertainty will vary substantially. The nature, timing and extent of the risk assessment and further audit procedures required by this ISA will vary in relation to the estimation uncertainty and the assessment of the related risks of material misstatement. For certain accounting estimates, estimation uncertainty may be very low, based on their nature, and the complexity and subjectivity involved in making them may also be very low. For such accounting estimates, the risk assessment procedures and further audit procedures required by this ISA would not be expected to be extensive. When estimation uncertainty, complexity or subjectivity

¹ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

² ISA 330, *The Auditor's Responses to Assessed Risks*

³ ISA 450, *Evaluation of Misstatements Identified during the Audit*

⁴ ISA 500, *Audit Evidence*

are very high, such procedures would be expected to be much more extensive. This ISA contains guidance on how the requirements of this ISA can be scaled. (Ref: Para. A7)

Key Concepts of This ISA

4. This ISA requires a separate assessment of inherent risk for purposes of assessing the risks of material misstatement at the assertion level for accounting estimates. Depending on the nature of a particular accounting estimate, the susceptibility of an assertion to a misstatement that could be material may be subject to or affected by estimation uncertainty, complexity, subjectivity or other inherent risk factors, and the interrelationship among them. As explained in ISA 200,⁵ inherent risk is higher for some assertions and related classes of transactions, account balances and disclosures than for others. Accordingly, the assessment of inherent risk depends on the degree to which the inherent risk factors affect the likelihood or magnitude of misstatement, and varies on a scale that is referred to in this ISA as the spectrum of inherent risk. (Ref: Para. A8–A9, A65–A66, Appendix 1)
5. This ISA refers to relevant requirements in ISA 315 (Revised) and ISA 330, and provides related guidance, to emphasize the importance of the auditor's decisions about controls relating to accounting estimates, including decisions about whether:
 - There are controls relevant to the audit, for which the auditor is required to evaluate their design and determine whether they have been implemented.
 - To test the operating effectiveness of relevant controls.
6. This ISA also requires a separate assessment of control risk when assessing the risks of material misstatement at the assertion level for accounting estimates. In assessing control risk, the auditor takes into account whether the auditor's further audit procedures contemplate planned reliance on the operating effectiveness of controls. If the auditor does not perform tests of controls, the auditor's assessment of the risk of material misstatement at the assertion level cannot be reduced for the effective operation of controls with respect to the particular assertion.⁶ (Ref: Para. A10)
7. This ISA emphasizes that the auditor's further audit procedures (including, where appropriate, tests of controls) need to be responsive to the reasons for the assessed risks of material misstatement at the assertion level, taking into account the effect of one or more inherent risk factors and the auditor's assessment of control risk.
8. The exercise of professional skepticism in relation to accounting estimates is affected by the auditor's consideration of inherent risk factors, and its importance increases when accounting estimates are subject to a greater degree of estimation uncertainty or are affected to a greater degree by complexity, subjectivity or other inherent risk factors. Similarly, the exercise of professional skepticism is important when there is greater susceptibility to misstatement due to management bias or fraud. (Ref: Para. A11)
9. This ISA requires the auditor to evaluate, based on the audit procedures performed and the audit evidence obtained, whether the accounting estimates and related disclosures are reasonable⁷ in the context of the applicable financial reporting framework, or are misstated. For purposes of this ISA, reasonable in the context of the applicable financial reporting framework means that the

⁵ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph A40

⁶ ISA 530, *Audit Sampling*, Appendix 3

⁷ See also ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 13(c)

relevant requirements of the applicable financial reporting framework have been applied appropriately, including those that address: (Ref: Para. A12–A13, A139–A144)

- The making of the accounting estimate, including the selection of the method, assumptions and data in view of the nature of the accounting estimate and the facts and circumstances of the entity;
- The selection of management's point estimate; and
- The disclosures about the accounting estimate, including disclosures about how the accounting estimate was developed and that explain the nature, extent, and sources of estimation uncertainty.

Effective Date

10. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2019.

Objective

11. The objective of the auditor is to obtain sufficient appropriate audit evidence about whether accounting estimates and related disclosures in the financial statements are reasonable in the context of the applicable financial reporting framework.

Definitions

12. For purposes of the ISAs, the following terms have the meanings attributed below:
- (a) Accounting estimate – A monetary amount for which the measurement, in accordance with the requirements of the applicable financial reporting framework, is subject to estimation uncertainty. (Ref: Para. A14)
 - (b) Auditor's point estimate or auditor's range – An amount, or range of amounts, respectively, developed by the auditor in evaluating management's point estimate. (Ref: Para. A15)
 - (c) Estimation uncertainty – Susceptibility to an inherent lack of precision in measurement. (Ref: Para. A16, Appendix 1)
 - (d) Management bias – A lack of neutrality by management in the preparation of information. (Ref: Para. A17)
 - (e) Management's point estimate – The amount selected by management for recognition or disclosure in the financial statements as an accounting estimate.
 - (f) Outcome of an accounting estimate – The actual monetary amount that results from the resolution of the transaction(s), event(s) or condition(s) addressed by an accounting estimate. (Ref: Para. A18)

Requirements

Risk Assessment Procedures and Related Activities

13. When obtaining an understanding of the entity and its environment, including the entity's internal control, as required by ISA 315 (Revised),⁸ the auditor shall obtain an understanding of the following matters related to the entity's accounting estimates. The auditor's procedures to obtain

⁸ ISA 315 (Revised), paragraphs 3, 5–6, 9, 11–12, 15–17, and 20–21

the understanding shall be performed to the extent necessary to provide an appropriate basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. (Ref: Para. A19–A22)

The Entity and Its Environment

- (a) The entity's transactions and other events and conditions that may give rise to the need for, or changes in, accounting estimates to be recognized or disclosed in the financial statements. (Ref: Para. A23)
- (b) The requirements of the applicable financial reporting framework related to accounting estimates (including the recognition criteria, measurement bases, and the related presentation and disclosure requirements); and how they apply in the context of the nature and circumstances of the entity and its environment, including how transactions and other events or conditions are subject to, or affected by, inherent risk factors. (Ref: Para. A24–A25)
- (c) Regulatory factors relevant to the entity's accounting estimates, including, when applicable, regulatory frameworks related to prudential supervision. (Ref: Para. A26)
- (d) The nature of the accounting estimates and related disclosures that the auditor expects to be included in the entity's financial statements, based on the auditor's understanding of the matters in 13(a)–(c) above. (Ref: Para. A27)

The Entity's Internal Control

- (e) The nature and extent of oversight and governance that the entity has in place over management's financial reporting process relevant to accounting estimates. (Ref: Para. A28–A30).
- (f) How management identifies the need for, and applies, specialized skills or knowledge related to accounting estimates, including with respect to the use of a management's expert. (Ref: Para. A31)
- (g) How the entity's risk assessment process identifies and addresses risks relating to accounting estimates. (Ref: Para. A32–A33)
- (h) The entity's information system as it relates to accounting estimates, including:
 - (i) The classes of transactions, events and conditions, that are significant to the financial statements and that give rise to the need for, or changes in, accounting estimates and related disclosures; and (Ref: Para. A34–A35)
 - (ii) For such accounting estimates and related disclosures, how management:
 - a. Identifies the relevant methods, assumptions or sources of data, and the need for changes in them, that are appropriate in the context of the applicable financial reporting framework, including how management: (Ref: Para. A36–A37)
 - i. Selects or designs, and applies, the methods used, including the use of models; (Ref: Para. A38–A39)
 - ii. Selects the assumptions to be used, including consideration of alternatives, and identifies significant assumptions; (Ref: Para. A40–A43); and

- iii. Selects the data to be used; (Ref: Para. A44)
 - b. Understands the degree of estimation uncertainty, including through considering the range of possible measurement outcomes; and (Ref: Para. A45)
 - c. Addresses the estimation uncertainty, including selecting a point estimate and related disclosures for inclusion in the financial statements. (Ref: Para. A46–A49)
 - (i) Control activities relevant to the audit over management's process for making accounting estimates as described in paragraph 13(h)(ii). (Ref: Para. A50–A54)
 - (j) How management reviews the outcome(s) of previous accounting estimates and responds to the results of that review.
14. The auditor shall review the outcome of previous accounting estimates, or, where applicable, their subsequent re-estimation to assist in identifying and assessing the risks of material misstatement in the current period. The auditor shall take into account the characteristics of the accounting estimates in determining the nature and extent of that review. The review is not intended to call into question judgments about previous period accounting estimates that were appropriate based on the information available at the time they were made. (Ref: Para. A55–A60)
15. With respect to accounting estimates, the auditor shall determine whether the engagement team requires specialized skills or knowledge to perform the risk assessment procedures, to identify and assess the risks of material misstatement, to design and perform audit procedures to respond to those risks, or to evaluate the audit evidence obtained. (Ref: Para. A61–A63)

Identifying and Assessing the Risks of Material Misstatement

16. In identifying and assessing the risks of material misstatement relating to an accounting estimate and related disclosures at the assertion level, as required by ISA 315 (Revised),⁹ the auditor shall separately assess inherent risk and control risk. The auditor shall take the following into account in identifying the risks of material misstatement and in assessing inherent risk: (Ref: Para. A64–A71)
- (a) The degree to which the accounting estimate is subject to estimation uncertainty; and (Ref: Para. A72–A75)
 - (b) The degree to which the following are affected by complexity, subjectivity, or other inherent risk factors: (Ref: Para. A76–A79)
 - (i) The selection and application of the method, assumptions and data in making the accounting estimate; or
 - (ii) The selection of management's point estimate and related disclosures for inclusion in the financial statements.
17. The auditor shall determine whether any of the risks of material misstatement identified and assessed in accordance with paragraph 16 are, in the auditor's judgment, a significant risk.¹⁰ If

⁹ ISA 315 (Revised), paragraph 25 and 26

¹⁰ ISA 315 (Revised), paragraph 27

the auditor has determined that a significant risk exists, the auditor shall obtain an understanding of the entity's controls, including control activities, relevant to that risk.¹¹ (Ref: Para. A80)

Responses to the Assessed Risks of Material Misstatement

18. As required by ISA 330,¹² the auditor's further audit procedures shall be responsive to the assessed risks of material misstatement at the assertion level,¹³ considering the reasons for the assessment given to those risks. The auditor's further audit procedures shall include one or more of the following approaches:

- (a) Obtaining audit evidence from events occurring up to the date of the auditor's report (see paragraph 21);
- (b) Testing how management made the accounting estimate (see paragraphs 22–27); or
- (c) Developing an auditor's point estimate or range (see paragraphs 28–29).

The auditor's further audit procedures shall take into account that the higher the assessed risk of material misstatement, the more persuasive the audit evidence needs to be.¹⁴ The auditor shall design and perform further audit procedures in a manner that is not biased towards obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory. (Ref: Para. A81–A84)

19. As required by ISA 330,¹⁵ the auditor shall design and perform tests to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls, if:

- (a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively, or
- (b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.

In relation to accounting estimates, the auditor's tests of such controls shall be responsive to the reasons for the assessment given to the risks of material misstatement. In designing and performing tests of controls, the auditor shall obtain more persuasive audit evidence the greater the reliance the auditor places on the effectiveness of a control.¹⁶ (Ref: Para. A85–A89)

20. For a significant risk relating to an accounting estimate, the auditor's further audit procedures shall include tests of controls in the current period if the auditor plans to rely on those controls. When the approach to a significant risk consists only of substantive procedures, those procedures shall include tests of details.¹⁷ (Ref: Para. A90)

Obtaining Audit Evidence from Events Occurring up to the Date of the Auditor's Report

21. When the auditor's further audit procedures include obtaining audit evidence from events occurring up to the date of the auditor's report, the auditor shall evaluate whether such audit evidence is sufficient and appropriate to address the risks of material misstatement relating to the

¹¹ ISA 315 (Revised), paragraph 29

¹² ISA 330, paragraphs 6–15 and 18

¹³ ISA 330, paragraphs 6–7 and 21

¹⁴ ISA 330, paragraph 7(b)

¹⁵ ISA 330, paragraph 8

¹⁶ ISA 330, paragraph 9

¹⁷ ISA 330, paragraphs 15 and 21

accounting estimate, taking into account that changes in circumstances and other relevant conditions between the event and the measurement date may affect the relevance of such audit evidence in the context of the applicable financial reporting framework. (Ref: Para. A91–A93)

Testing How Management Made the Accounting Estimate

22. When testing how management made the accounting estimate, the auditor's further audit procedures shall include procedures, designed and performed in accordance with paragraphs 23–26, to obtain sufficient appropriate audit evidence regarding the risks of material misstatement relating to: (Ref: Para. A94)
- (a) The selection and application of the methods, significant assumptions and the data used by management in making the accounting estimate; and
 - (b) How management selected the point estimate and developed related disclosures about estimation uncertainty.

Methods

23. In applying the requirements of paragraph 22, with respect to methods, the auditor's further audit procedures shall address:
- (a) Whether the method selected is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from the method used in prior periods are appropriate; (Ref: Para. A95, A97)
 - (b) Whether judgments made in selecting the method give rise to indicators of possible management bias; (Ref: Para. A96)
 - (c) Whether the calculations are applied in accordance with the method and are mathematically accurate;
 - (d) When management's application of the method involves complex modelling, whether judgments have been applied consistently and whether, when applicable: (Ref: Para. A98–A100)
 - (i) The design of the model meets the measurement objective of the applicable financial reporting framework, is appropriate in the circumstances, and, if applicable, changes from the prior period's model are appropriate in the circumstances; and
 - (ii) Adjustments to the output of the model are consistent with the measurement objective of the applicable financial reporting framework and are appropriate in the circumstances; and
 - (e) Whether the integrity of the significant assumptions and the data has been maintained in applying the method. (Ref: Para. A101)

Significant Assumptions

24. In applying the requirements of paragraph 22, with respect to significant assumptions, the auditor's further audit procedures shall address:
- (a) Whether the significant assumptions are appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate; (Ref: Para. A95, A102–A103)
 - (b) Whether judgments made in selecting the significant assumptions give rise to indicators of

possible management bias; (Ref: Para. A96)

- (c) Whether the significant assumptions are consistent with each other and with those used in other accounting estimates, or with related assumptions used in other areas of the entity's business activities, based on the auditor's knowledge obtained in the audit; and (Ref: Para. A104)
- (d) When applicable, whether management has the intent to carry out specific courses of action and has the ability to do so. (Ref: Para. A105)

Data

25. In applying the requirements of paragraph 22, with respect to data, the auditor's further audit procedures shall address:
- (a) Whether the data is appropriate in the context of the applicable financial reporting framework, and, if applicable, changes from prior periods are appropriate (Ref: Para. A95, A106);
 - (b) Whether judgments made in selecting the data give rise to indicators of possible management bias; (Ref: Para. A96)
 - (c) Whether the data is relevant and reliable in the circumstances; and (Ref: Para. A107)
 - (d) Whether the data has been appropriately understood or interpreted by management, including with respect to contractual terms. (Ref: Para. A108)

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

26. In applying the requirements of paragraph 22, the auditor's further audit procedures shall address whether, in the context of the applicable financial reporting framework, management has taken appropriate steps to:
- (a) Understand estimation uncertainty; and (Ref: Para. A109)
 - (b) Address estimation uncertainty by selecting an appropriate point estimate and by developing related disclosures about estimation uncertainty. (Ref: Para. A110–A114)
27. When, in the auditor's judgment based on the audit evidence obtained, management has not taken appropriate steps to understand or address estimation uncertainty, the auditor shall: (Ref: Para. A115–A117)
- (a) Request management to perform additional procedures to understand estimation uncertainty or to address it by reconsidering the selection of management's point estimate or considering providing additional disclosures relating to the estimation uncertainty, and evaluate management's response(s) in accordance with paragraph 26;
 - (b) If the auditor determines that management's response to the auditor's request does not sufficiently address estimation uncertainty, to the extent practicable, develop an auditor's point estimate or range in accordance with paragraphs 28–29; and
 - (c) Evaluate whether a deficiency in internal control exists and, if so, communicate in accordance with ISA 265.¹⁸

¹⁸ ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

Developing an Auditor's Point Estimate or Range

28. When the auditor develops a point estimate or range to evaluate management's point estimate and related disclosures about estimation uncertainty, including when required by paragraph 27(b), the auditor's further audit procedures shall include procedures to evaluate whether the methods, assumptions or data used are appropriate in the context of the applicable financial reporting framework. Regardless of whether the auditor uses management's or the auditor's own methods, assumptions or data, these further audit procedures shall be designed and performed to address the matters in paragraphs 23–25. (Ref: Para. A118–A123)
29. If the auditor develops an auditor's range, the auditor shall:
- (a) Determine that the range includes only amounts that are supported by sufficient appropriate audit evidence and have been evaluated by the auditor to be reasonable in the context of the measurement objectives and other requirements of the applicable financial reporting framework; and (Ref: Para. A124–A125)
 - (b) Design and perform further audit procedures to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement relating to the disclosures in the financial statements that describe the estimation uncertainty.

Other Considerations Relating to Audit Evidence

30. In obtaining audit evidence regarding the risks of material misstatement relating to accounting estimates, irrespective of the sources of information to be used as audit evidence, the auditor shall comply with the relevant requirements in ISA 500.

When using the work of a management's expert, the requirements in paragraphs 21–29 of this ISA may assist the auditor in evaluating the appropriateness of the expert's work as audit evidence for a relevant assertion in accordance with paragraph 8(c) of ISA 500. In evaluating the work of the management's expert, the nature, timing and extent of the further audit procedures are affected by the auditor's evaluation of the expert's competence, capabilities and objectivity, the auditor's understanding of the nature of the work performed by the expert, and the auditor's familiarity with the expert's field of expertise. (Ref: Para. A126–A132)

Disclosures Related to Accounting Estimates

31. The auditor shall design and perform further audit procedures to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement at the assertion level for disclosures related to an accounting estimate, other than those related to estimation uncertainty addressed in paragraphs 26(b) and 29(b).

Indicators of Possible Management Bias

32. The auditor shall evaluate whether judgments and decisions made by management in making the accounting estimates included in the financial statements, even if they are individually reasonable, are indicators of possible management bias. When indicators of possible management bias are identified, the auditor shall evaluate the implications for the audit. Where there is intention to mislead, management bias is fraudulent in nature. (Ref: Para. A133–A136)

Overall Evaluation Based on Audit Procedures Performed

33. In applying ISA 330 to accounting estimates,¹⁹ the auditor shall evaluate, based on the audit procedures performed and audit evidence obtained, whether: (Ref: Para A137–A138)
- (a) The assessments of the risks of material misstatement at the assertion level remain appropriate, including when indicators of possible management bias have been identified;
 - (b) Management's decisions relating to the recognition, measurement, presentation and disclosure of these accounting estimates in the financial statements are in accordance with the applicable financial reporting framework; and
 - (c) Sufficient appropriate audit evidence has been obtained.
34. In making the evaluation required by paragraph 33(c), the auditor shall take into account all relevant audit evidence obtained, whether corroborative or contradictory.²⁰ If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall evaluate the implications for the audit or the auditor's opinion on the financial statements in accordance with ISA 705 (Revised).²¹

Determining Whether the Accounting Estimates are Reasonable or Misstated

35. The auditor shall determine whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated. ISA 450²² provides guidance on how the auditor may distinguish misstatements (whether factual, judgmental, or projected) for the auditor's evaluation of the effect of uncorrected misstatements on the financial statements. (Ref: Para. A12–A13, A139–A144)
36. In relation to accounting estimates, the auditor shall evaluate:
- (a) In the case of a fair presentation framework, whether management has included disclosures, beyond those specifically required by the framework, that are necessary to achieve the fair presentation of the financial statements as a whole;²³ or
 - (b) In the case of a compliance framework, whether the disclosures are those that are necessary for the financial statements not to be misleading.²⁴

Written Representations

37. The auditor shall request written representations from management²⁵ and, when appropriate, those charged with governance about whether the methods, significant assumptions and the data used in making the accounting estimates and the related disclosures are appropriate to achieve recognition, measurement or disclosure that is in accordance with the applicable financial reporting framework. The auditor shall also consider the need to obtain representations about specific accounting estimates, including in relation to the methods, assumptions, or data used. (Ref: Para. A145)

¹⁹ ISA 330, paragraphs 25–26

²⁰ ISA 500, paragraph 11

²¹ ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

²² ISA 450, paragraph A6

²³ See also ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 14

²⁴ See also ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 19

²⁵ ISA 580, *Written Representations*

Communication with Those Charged With Governance, Management, or Other Relevant Parties

38. In applying ISA 260 (Revised)²⁶ and ISA 265,²⁷ the auditor is required to communicate with those charged with governance or management about certain matters, including significant qualitative aspects of the entity's accounting practices and significant deficiencies in internal control, respectively. In doing so, the auditor shall consider the matters, if any, to communicate regarding accounting estimates and take into account whether the reasons given to the risks of material misstatement relate to estimation uncertainty, or the effects of complexity, subjectivity or other inherent risk factors in making accounting estimates and related disclosures. In addition, in certain circumstances, the auditor is required by law or regulation to communicate about certain matters with other relevant parties, such as regulators or prudential supervisors. (Ref: Para. A146–A148)

Documentation

39. The auditor shall include in the audit documentation:²⁸ (Ref: Para. A149–A152)
- (a) Key elements of the auditor's understanding of the entity and its environment, including the entity's internal control related to the entity's accounting estimates;
 - (b) The linkage of the auditor's further audit procedures with the assessed risks of material misstatement at the assertion level,²⁹ taking into account the reasons (whether related to inherent risk or control risk) given to the assessment of those risks;
 - (c) The auditor's response(s) when management has not taken appropriate steps to understand and address estimation uncertainty;
 - (d) Indicators of possible management bias related to accounting estimates, if any, and the auditor's evaluation of the implications for the audit, as required by paragraph 32; and
 - (e) Significant judgments relating to the auditor's determination of whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated.

* * *

Application and Other Explanatory Material

Nature of Accounting Estimates (Ref: Para. 2)

Examples of Accounting Estimates

- A1. Examples of accounting estimates related to classes of transactions, account balances and disclosures include:
- Inventory obsolescence.
 - Depreciation of property and equipment.
 - Valuation of infrastructure assets.
 - Valuation of financial instruments.
 - Outcome of pending litigation.

²⁶ ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 16(a)

²⁷ ISA 265, paragraph 9

²⁸ ISA 230, *Audit Documentation*, paragraphs 8–11, A6, A7 and A10

²⁹ ISA 330, paragraph 28(b)

- Provision for expected credit losses.
- Valuation of insurance contract liabilities.
- Warranty obligations.
- Employee retirement benefits liabilities.
- Share-based payments.
- Fair value of assets or liabilities acquired in a business combination, including the determination of goodwill and intangible assets.
- Impairment of long-lived assets or property or equipment held for disposal.
- Non-monetary exchanges of assets or liabilities between independent parties.
- Revenue recognized for long-term contracts.

Methods

- A2. A method is a measurement technique used by management to make an accounting estimate in accordance with the required measurement basis. For example, one recognized method used to make accounting estimates relating to share-based payment transactions is to determine a theoretical option call price using the Black Scholes option pricing formula. A method is applied using a computational tool or process, sometimes referred to as a model, and involves applying assumptions and data and taking into account a set of relationships between them.

Assumptions and Data

- A3. Assumptions involve judgments based on available information about matters such as the choice of an interest rate, a discount rate, or judgments about future conditions or events. An assumption may be selected by management from a range of appropriate alternatives. Assumptions that may be made or identified by a management's expert become management's assumptions when used by management in making an accounting estimate.
- A4. For purposes of this ISA, data is information that can be obtained through direct observation or from a party external to the entity. Information obtained by applying analytical or interpretive techniques to data is referred to as derived data when such techniques have a well-established theoretical basis and therefore less need for management judgment. Otherwise, such information is an assumption.
- A5. Examples of data include:
- Prices agreed in market transactions;
 - Operating times or quantities of output from a production machine;
 - Historical prices or other terms included in contracts, such as a contracted interest rate, a payment schedule, and term included in a loan agreement;
 - Forward-looking information such as economic or earnings forecasts obtained from an external information source, or
 - A future interest rate determined using interpolation techniques from forward interest rates (derived data).
- A6. Data can come from a wide range of sources. For example, data can be:
- Generated within the organization or externally;

- Obtained from a system that is either within or outside the general or subsidiary ledgers;
- Observable in contracts; or
- Observable in legislative or regulatory pronouncements.

Scalability (Ref: Para. 3)

A7. Examples of paragraphs that include guidance on how the requirements of this ISA can be scaled include paragraphs A20–A22, A63, A67, and A84.

Key Concepts of This ISA

Inherent Risk Factors (Ref: Para. 4)

- A8. Inherent risk factors are characteristics of conditions and events that may affect the susceptibility of an assertion to misstatement, before consideration of controls. Appendix 1 further explains the nature of these inherent risk factors, and their inter-relationships, in the context of making accounting estimates and their presentation in the financial statements.
- A9. In addition to the inherent risk factors of estimation uncertainty, complexity or subjectivity, other inherent risk factors that the auditor may consider in identifying and assessing the risks of material misstatement may include the extent to which the accounting estimate is subject to, or affected by:
- Change in the nature or circumstances of the relevant financial statement items, or requirements of the applicable financial reporting framework which may give rise to the need for changes in the method, assumptions or data used to make the accounting estimate.
 - Susceptibility to misstatement due to management bias or fraud in making the accounting estimate.

Control Risk (Ref: Para. 6)

A10. An important consideration for the auditor in assessing control risk at the assertion level is the effectiveness of the design of the controls that the auditor intends to rely on and the extent to which the controls address the assessed inherent risks at the assertion level. The auditor's evaluation that controls are effectively designed and have been implemented supports an expectation about the operating effectiveness of the controls in determining whether to test them.

Professional Skepticism (Ref: Para. 8)

A11. Paragraphs A60, A95, A96, A137 and A139 are examples of paragraphs that describe ways in which the auditor can exercise professional skepticism. Paragraph A152 provides guidance on ways in which the auditor's exercise of professional skepticism may be documented, and includes examples of specific paragraphs in this ISA for which documentation may provide evidence of the exercise of professional skepticism.

Concept of "Reasonable" (Ref: Para. 9, 35)

A12. Other considerations that may be relevant to the auditor's consideration of whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework include whether:

- The data and assumptions used in making the accounting estimate are consistent with each other and with those used in other accounting estimates or areas of the entity's business activities; and
- The accounting estimate takes into account appropriate information as required by the applicable financial reporting framework.

A13. The term “applied appropriately” as used in paragraph 9 means in a manner that not only complies with the requirements of the applicable financial reporting framework but, in doing so, reflects judgments that are consistent with the objective of the measurement basis in that framework.

Definitions

Accounting Estimate (Ref: Para. 12(a))

A14. Accounting estimates are monetary amounts that may be related to classes of transactions or account balances recognized or disclosed in the financial statements. Accounting estimates also include monetary amounts included in disclosures or used to make judgments about recognition or disclosure relating to a class of transactions or account balance.

Auditor's Point Estimate or Auditor's Range (Ref: Para. 12(b))

A15. An auditor's point estimate or range may be used to evaluate an accounting estimate directly (for example, an impairment provision or the fair value of different types of financial instruments), or indirectly (for example, an amount to be used as a significant assumption for an accounting estimate). A similar approach may be taken by the auditor in developing an amount or range of amounts in evaluating a non-monetary item of data or an assumption (for example, an estimated useful life of an asset).

Estimation Uncertainty (Ref: Para. 12(c))

A16. Not all accounting estimates are subject to a high degree of estimation uncertainty. For example, some financial statement items may have an active and open market that provides readily available and reliable information on the prices at which actual exchanges occur. However, estimation uncertainty may exist even when the valuation method and data are well defined. For example, valuation of securities quoted on an active and open market at the listed market price may require adjustment if the holding is significant or is subject to restrictions in marketability. In addition, general economic circumstances prevailing at the time, for example, illiquidity in a particular market, may impact estimation uncertainty.

Management Bias (Ref: Para. 12(d))

A17. Financial reporting frameworks often call for neutrality, that is, freedom from bias. Estimation uncertainty gives rise to subjectivity in making an accounting estimate. The presence of subjectivity gives rise to the need for judgment by management and the susceptibility to unintentional or intentional management bias (for example, as a result of motivation to achieve a desired profit target or capital ratio). The susceptibility of an accounting estimate to management bias increases with the extent to which there is subjectivity in making the accounting estimate.

Outcome of an Accounting Estimate (Ref: Para. 12(f))

A18. Some accounting estimates, by their nature, do not have an outcome that is relevant for the auditor's work performed in accordance with this ISA. For example, an accounting estimate may

be based on perceptions of market participants at a point in time. Accordingly, the price realized when an asset is sold or a liability is transferred may differ from the related accounting estimate made at the reporting date because, with the passage of time, the market participants' perceptions of value have changed.

Risk Assessment Procedures and Related Activities

Obtaining an Understanding of the Entity and Its Environment (Ref: Para. 13)

A19. Paragraphs 11–24 of ISA 315 (Revised) require the auditor to obtain an understanding of certain matters about the entity and its environment, including the entity's internal control. The requirements in paragraph 13 of this ISA relate more specifically to accounting estimates and build on the broader requirements in ISA 315 (Revised).

Scalability

A20. The nature, timing, and extent of the auditor's procedures to obtain the understanding of the entity and its environment, including the entity's internal control, related to the entity's accounting estimates, may depend, to a greater or lesser degree, on the extent to which the individual matter(s) apply in the circumstances. For example, the entity may have few transactions or other events and conditions that give rise to the need for accounting estimates, the applicable financial reporting requirements may be simple to apply, and there may be no relevant regulatory factors. Further, the accounting estimates may not require significant judgments, and the process for making the accounting estimates may be less complex. In these circumstances, the accounting estimates may be subject to or affected by estimation uncertainty, complexity, subjectivity, or other inherent risk factors to a lesser degree and there may be fewer controls relevant to the audit. If so, the auditor's risk assessment procedures are likely to be less extensive and may be obtained primarily through inquiries of management with appropriate responsibilities for the financial statements and simple walk-throughs of management's process for making the accounting estimate.

A21. By contrast, the accounting estimates may require significant judgments by management, and the process for making the accounting estimates may be complex and involve the use of complex models. In addition, the entity may have a more sophisticated information system, and more extensive controls over accounting estimates. In these circumstances, the accounting estimates may be subject to or affected by estimation uncertainty, subjectivity, complexity or other inherent risk factors to a greater degree. If so, the nature or timing of the auditor's risk assessment procedures are likely to be different, or be more extensive, than in the circumstances in paragraph A20.

A22. The following considerations may be relevant for entities with only simple businesses, which may include many smaller entities:

- Processes relevant to accounting estimates may be uncomplicated because the business activities are simple or the required estimates may have a lesser degree of estimation uncertainty.
- Accounting estimates may be generated outside of the general and subsidiary ledgers, controls over their development may be limited, and an owner-manager may have significant influence over their determination. The owner-manager's role in making the accounting estimates may need to be taken into account by the auditor both when identifying the risks of material misstatement and when considering the risk of management bias.

The Entity and Its Environment

The entity's transactions and other events and conditions (Ref: Para. 13(a))

A23. Changes in circumstances that may give rise to the need for, or changes in, accounting estimates may include, for example, whether:

- The entity has engaged in new types of transactions;
- Terms of transactions have changed; or
- New events or conditions have occurred.

The requirements of the applicable financial reporting framework (Ref: Para. 13(b))

A24. Obtaining an understanding of the requirements of the applicable financial reporting framework provides the auditor with a basis for discussion with management and, where applicable, those charged with governance about how management has applied those requirements relevant to the accounting estimates, and about the auditor's determination of whether they have been applied appropriately. This understanding also may assist the auditor in communicating with those charged with governance when the auditor considers a significant accounting practice that is acceptable under the applicable financial reporting framework, not to be the most appropriate in the circumstances of the entity.³⁰

A25. In obtaining this understanding, the auditor may seek to understand whether:

- The applicable financial reporting framework:
 - Prescribes certain criteria for the recognition, or methods for the measurement of accounting estimates;
 - Specifies certain criteria that permit or require measurement at a fair value, for example, by referring to management's intentions to carry out certain courses of action with respect to an asset or liability; or
 - Specifies required or suggested disclosures, including disclosures concerning judgments, assumptions, or other sources of estimation uncertainty relating to accounting estimates; and
- Changes in the applicable financial reporting framework require changes to the entity's accounting policies relating to accounting estimates.

Regulatory factors (Ref: Para. 13(c))

A26. Obtaining an understanding of regulatory factors, if any, that are relevant to accounting estimates may assist the auditor in identifying applicable regulatory frameworks (for example, regulatory frameworks established by prudential supervisors in the banking or insurance industries) and in determining whether such regulatory framework(s):

- Addresses conditions for the recognition, or methods for the measurement, of accounting estimates, or provides related guidance thereon;
- Specifies, or provides guidance about, disclosures in addition to the requirements of the applicable financial reporting framework;

³⁰ ISA 260 (Revised), paragraph 16(a)

- Provides an indication of areas for which there may be a potential for management bias to meet regulatory requirements; or
- Contains requirements for regulatory purposes that are not consistent with requirements of the applicable financial reporting framework, which may indicate potential risks of material misstatement. For example, some regulators may seek to influence minimum levels for expected credit loss provisions that exceed those required by the applicable financial reporting framework.

The nature of the accounting estimates and related disclosures that the auditor expects to be included in the financial statements (Ref: Para. 13(d))

A27. Obtaining an understanding of the nature of accounting estimates and related disclosures that the auditor expects to be included in the entity's financial statements assists the auditor in understanding the measurement basis of such accounting estimates and the nature and extent of disclosures that may be relevant. Such an understanding provides the auditor with a basis for discussion with management about how management makes the accounting estimates.

The Entity's Internal Control Relevant to the Audit

The nature and extent of oversight and governance (Ref: Para. 13(e))

A28. In applying ISA 315 (Revised),³¹ the auditor's understanding of the nature and extent of oversight and governance that the entity has in place over management's process for making accounting estimates may be important to the auditor's required evaluation as it relates to whether:

- Management, with the oversight of those charged with governance, has created and maintained a culture of honesty and ethical behavior; and
- The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control and whether those other components are undermined by deficiencies in the control environment.

A29. The auditor may obtain an understanding of whether those charged with governance:

- Have the skills or knowledge to understand the characteristics of a particular method or model to make accounting estimates, or the risks related to the accounting estimate, for example, risks related to the method or information technology used in making the accounting estimates;
- Have the skills and knowledge to understand whether management made the accounting estimates in accordance with the applicable financial reporting framework;
- Are independent from management, have the information required to evaluate on a timely basis how management made the accounting estimates, and the authority to call into question management's actions when those actions appear to be inadequate or inappropriate;
- Oversee management's process for making the accounting estimates, including the use of models; or
- Oversee the monitoring activities undertaken by management. This may include supervision and review procedures designed to detect and correct any deficiencies in the design or operating effectiveness of controls over the accounting estimates.

³¹ ISA 315 (Revised), paragraph 14

A30. Obtaining an understanding of the oversight by those charged with governance may be important when there are accounting estimates that:

- Require significant judgment by management to address subjectivity;
- Have high estimation uncertainty;
- Are complex to make, for example, because of the extensive use of information technology, large volumes of data or the use of multiple data sources or assumptions with complex interrelationships;
- Had, or ought to have had, a change in the method, assumptions or data compared to previous periods; or
- Involve significant assumptions.

Management's application of specialized skills or knowledge, including the use of management's experts (Ref: Para. 13(f))

A31. The auditor may consider whether the following circumstances increase the likelihood that management needs to engage an expert:³²

- The specialized nature of the matter requiring estimation, for example, the accounting estimate may involve measurement of mineral or hydrocarbon reserves in extractive industries or the evaluation of the likely outcome of applying complex contractual terms.
- The complex nature of the models required to apply the relevant requirements of the applicable financial reporting framework, as may be the case in certain measurements, such as level 3 fair values.³³
- The unusual or infrequent nature of the condition, transaction or event requiring an accounting estimate.

The entity's risk assessment process (Ref: Para. 13(g))

A32. Understanding how the entity's risk assessment process identifies and addresses risks relating to accounting estimates may assist the auditor in considering changes in:

- The requirements of the applicable financial reporting framework related to the accounting estimates;
- The availability or nature of data sources that are relevant to making the accounting estimates or that may affect the reliability of the data used;
- The entity's information system or IT environment; and
- Key personnel.

A33. Matters that the auditor may consider in obtaining an understanding of how management identified and addresses the susceptibility to misstatement due to management bias or fraud in making accounting estimates, include whether, and if so how, management:

- Pays particular attention to selecting or applying the methods, assumptions and data used in making accounting estimates.

³² ISA 500, paragraph 8

³³ See, for example, International Financial Reporting Standard (IFRS) 13, *Fair Value Measurement*.

- Monitors key performance indicators that may indicate unexpected or inconsistent performance compared with historical or budgeted performance or with other known factors.
- Identifies financial or other incentives that may be a motivation for bias.
- Monitors the need for changes in the methods, significant assumptions or the data used in making accounting estimates.
- Establishes appropriate oversight and review of models used in making accounting estimates.
- Requires documentation of the rationale for, or an independent review of, significant judgments made in making accounting estimates.

The entity's information system relating to accounting estimates (Ref: Para. 13(h)(i))

A34. The classes of transactions, events and conditions within the scope of paragraph 13(h) are the same as the classes of transactions, events and conditions relating to accounting estimates and related disclosures that are subject to paragraphs 18(a) and (d) of ISA 315 (Revised). In obtaining the understanding of the entity's information system as it relates to accounting estimates, the auditor may consider:

- Whether the accounting estimates arise from the recording of routine and recurring transactions or whether they arise from non-recurring or unusual transactions.
- How the information system addresses the completeness of accounting estimates and related disclosures, in particular for accounting estimates related to liabilities.

A35. During the audit, the auditor may identify classes of transactions, events and conditions that give rise to the need for accounting estimates and related disclosures that management failed to identify. ISA 315 (Revised) deals with circumstances where the auditor identifies risks of material misstatement that management failed to identify, including determining whether there is a significant deficiency in internal control with regard to the entity's risk assessment process.³⁴

Management's Identification of the Relevant Methods, Assumptions and Sources of Data (Ref: Para. 13(h)(ii)(a))

A36. If management has changed the method for making an accounting estimate, considerations may include whether the new method is, for example, more appropriate, is itself a response to changes in the environment or circumstances affecting the entity, or to changes in the requirements of the applicable financial reporting framework or regulatory environment, or whether management has another valid reason.

A37. If management has not changed the method for making an accounting estimate, considerations may include whether the continued use of the previous methods, assumptions and data is appropriate in view of the current environment or circumstances.

Methods (Ref: Para. 13(h)(ii)(a)(i))

A38. The applicable financial reporting framework may prescribe the method to be used in making an accounting estimate. In many cases, however, the applicable financial reporting framework does not prescribe a single method, or the required measurement basis prescribes, or allows, the use of alternative methods.

³¹ ISA 315 (Revised), paragraph 17

Models

A39. Management may design and implement specific controls around models used for making accounting estimates, whether management's own model or an external model. When the model itself has an increased level of complexity or subjectivity, such as an expected credit loss model or a fair value model using level 3 inputs, controls that address such complexity or subjectivity may be more likely to be identified as relevant to the audit. When complexity in relation to models is present, controls over data integrity are also more likely to be relevant to the audit. Factors that may be appropriate for the auditor to consider in obtaining an understanding of the model and of control activities relevant to the audit include the following:

- How management determines the relevance and accuracy of the model;
- The validation or back testing of the model, including whether the model is validated prior to use and revalidated at regular intervals to determine whether it remains suitable for its intended use. The entity's validation of the model may include evaluation of:
 - The model's theoretical soundness;
 - The model's mathematical integrity; and
 - The accuracy and completeness of the data and the appropriateness of data and assumptions used in the model.
- How the model is appropriately changed or adjusted on a timely basis for changes in market or other conditions and whether there are appropriate change control policies over the model;
- Whether adjustments, also referred to as overlays in certain industries, are made to the output of the model and whether such adjustments are appropriate in the circumstances in accordance with the requirements of the applicable financial reporting framework. When the adjustments are not appropriate, such adjustments may be indicators of possible management bias; and
- Whether the model is adequately documented, including its intended applications, limitations, key parameters, required data and assumptions, the results of any validation performed on it and the nature of, and basis for, any adjustments made to its output.

Assumptions (Ref: Para. 13(h)(ii)(a)(ii))

A40. Matters that the auditor may consider in obtaining an understanding of how management selected the assumptions used in making the accounting estimates include, for example:

- The basis for management's selection and the documentation supporting the selection of the assumption. The applicable financial reporting framework may provide criteria or guidance to be used in the selection of an assumption.
- How management assesses whether the assumptions are relevant and complete.
- When applicable, how management determines that the assumptions are consistent with each other, with those used in other accounting estimates or areas of the entity's business activities, or with other matters that are:
 - Within the control of management (for example, assumptions about the maintenance programs that may affect the estimation of an asset's useful life), and whether they are consistent with the entity's business plans and the external environment; and

- Outside the control of management (for example, assumptions about interest rates, mortality rates or potential judicial or regulatory actions).
- The requirements of the applicable financial reporting framework related to the disclosure of assumptions.

A41. With respect to fair value accounting estimates, assumptions vary in terms of the sources of the data and the basis for the judgments to support them, as follows:

- (a) Those that reflect what marketplace participants would use in pricing an asset or liability, developed based on market data obtained from sources independent of the reporting entity.
- (b) Those that reflect the entity's own judgments about what assumptions marketplace participants would use in pricing the asset or liability, developed based on the best data available in the circumstances.

In practice, however, the distinction between (a) and (b) may not always be apparent and distinguishing between them depends on understanding the sources of data and the basis for the judgments that support the assumption. Further, it may be necessary for management to select from a number of different assumptions used by different marketplace participants.

A42. Assumptions used in making an accounting estimate are referred to as significant assumptions in this ISA if a reasonable variation in the assumption would materially affect the measurement of the accounting estimate. A sensitivity analysis may be useful in demonstrating the degree to which the measurement varies based on one or more assumptions used in making the accounting estimate.

Inactive or illiquid markets

A43. When markets are inactive or illiquid, the auditor's understanding of how management selects assumptions may include understanding whether management has:

- Implemented appropriate policies for adapting the application of the method in such circumstances. Such adaptation may include making model adjustments or developing new models that are appropriate in the circumstances;
- Resources with the necessary skills or knowledge to adapt or develop a model, if necessary on an urgent basis, including selecting the valuation technique that is appropriate in such circumstances;
- The resources to determine the range of outcomes, given the uncertainties involved, for example by performing a sensitivity analysis;
- The means to assess how, when applicable, the deterioration in market conditions has affected the entity's operations, environment and relevant business risks and the implications for the entity's accounting estimates, in such circumstances; and
- An appropriate understanding of how the price data, and the relevance thereof, from particular external information sources may vary in such circumstances.

Data (Ref: Para. 13(h)(ii)(a)(iii))

A44. Matters that the auditor may consider in obtaining an understanding of how management selects the data on which the accounting estimates are based include:

- The nature and source of the data, including information obtained from an external information source.

- How management evaluates whether the data is appropriate.
- The accuracy and completeness of the data.
- The consistency of the data used with data used in previous periods.
- The complexity of the information technology systems used to obtain and process the data, including when this involves handling large volumes of data.
- How the data is obtained, transmitted and processed and how its integrity is maintained.

How management understands and addresses estimation uncertainty (Ref: Para. 13(h)(ii)(b)–13(h)(ii)(c))

A45. Matters that may be appropriate for the auditor to consider relating to whether and how management understands the degree of estimation uncertainty include, for example:

- Whether, and if so, how management identified alternative methods, significant assumptions or sources of data that are appropriate in the context of the applicable financial reporting framework.
- Whether, and if so, how management considered alternative outcomes by, for example, performing a sensitivity analysis to determine the effect of changes in the significant assumptions or the data used in making the accounting estimate.

A46. The requirements of the applicable financial reporting framework may specify the approach to selecting management's point estimate from the reasonably possible measurement outcomes. Financial reporting frameworks may recognize that the appropriate amount is one that is appropriately selected from the reasonably possible measurement outcomes and, in some cases, may indicate that the most relevant amount may be in the central part of that range.

A47. For example, with respect to fair value estimates, IFRS³⁵ indicates that, if multiple valuation techniques are used to measure fair value, the results (i.e., respective indications of fair value) shall be evaluated considering the reasonableness of the range of values indicated by those results. A fair value measurement is the point within that range that is most representative of fair value in the circumstances. In other cases, the applicable financial reporting framework may specify the use of a probability-weighted average of the reasonably possible measurement outcomes, or of the measurement amount that is most likely or that is more likely than not.

A48. The applicable financial reporting framework may prescribe disclosures or disclosure objectives related to accounting estimates, and some entities may choose to disclose additional information. These disclosures or disclosure objectives may address, for example:

- The method of estimation used, including any applicable model and the basis for its selection.
- Information that has been obtained from models, or from other calculations used to determine estimates recognized or disclosed in the financial statements, including information relating to the underlying data and assumptions used in those models, such as:
 - Assumptions developed internally; or
 - Data, such as interest rates, that are affected by factors outside the control of the entity.

³⁵ IFRS 13, Fair Value Measurement, paragraph 63

- The effect of any changes to the method of estimation from the prior period.
- The sources of estimation uncertainty.
- Fair value information.
- Information about sensitivity analyses derived from financial models that demonstrates that management has considered alternative assumptions.

A49. In some cases, the applicable financial reporting framework may require specific disclosures regarding estimation uncertainty, for example:

- The disclosure of information about the assumptions made about the future and other major sources of estimation uncertainty that give rise to a higher likelihood or magnitude of material adjustment to the carrying amounts of assets and liabilities after the period end. Such requirements may be described using terms such as “Key Sources of Estimation Uncertainty” or “Critical Accounting Estimates.” They may relate to accounting estimates that require management’s most difficult, subjective or complex judgments. Such judgments may be more subjective and complex, and accordingly the potential for a consequential material adjustment to the carrying amounts of assets and liabilities may increase, with the number of items of data and assumptions affecting the possible future resolution of the estimation uncertainty. Information that may be disclosed includes:
 - The nature of the assumption or other source of estimation uncertainty;
 - The sensitivity of carrying amounts to the methods and assumptions used, including the reasons for the sensitivity;
 - The expected resolution of an uncertainty and the range of reasonably possible outcomes in respect of the carrying amounts of the assets and liabilities affected; and
 - An explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved.
- The disclosure of the range of possible outcomes, and the assumptions used in determining the range.
- The disclosure of specific information, such as:
 - Information regarding the significance of fair value accounting estimates to the entity’s financial position and performance; and
 - Disclosures regarding market inactivity or illiquidity.
- Qualitative disclosures such as the exposures to risk and how they arise, the entity’s objectives, policies and procedures for managing the risk and the methods used to measure the risk and any changes from the previous period of these qualitative concepts.
- Quantitative disclosures such as the extent to which the entity is exposed to risk, based on information provided internally to the entity’s key management personnel, including credit risk, liquidity risk and market risk.

Control Activities Relevant to the Audit Over Management’s Process for Making Accounting Estimates (Ref: Para 13(i))

A50. The auditor’s judgment in identifying controls relevant to the audit, and therefore the need to evaluate the design of those controls and determine whether they have been implemented,

relates to management's process described in paragraph 13(h)(ii). The auditor may not identify relevant control activities in relation to all the elements of paragraph 13(h)(ii), depending on the complexity associated with the accounting estimate.

A51. As part of obtaining an understanding of the control activities relevant to the audit, the auditor may consider:

- How management determines the appropriateness of the data used to develop the accounting estimates, including when management uses an external information source or data from outside the general and subsidiary ledgers.
- The review and approval of accounting estimates, including the assumptions or data used in their development, by appropriate levels of management and, where appropriate, those charged with governance.
- The segregation of duties between those responsible for making the accounting estimates and those committing the entity to the related transactions, including whether the assignment of responsibilities appropriately takes account of the nature of the entity and its products or services. For example, in the case of a large financial institution, relevant segregation of duties may consist of an independent function responsible for estimation and validation of fair value pricing of the entity's financial products staffed by individuals whose remuneration is not tied to such products.
- The effectiveness of the design of the control activities. Generally, it may be more difficult for management to design controls that address subjectivity and estimation uncertainty in a manner that effectively prevents, or detects and corrects, material misstatements, than it is to design controls that address complexity. Controls that address subjectivity and estimation uncertainty may need to include more manual elements, which may be less reliable than automated controls as they can be more easily bypassed, ignored or overridden by management. The design effectiveness of controls addressing complexity may vary depending on the reason for, and the nature of, the complexity. For example, it may be easier to design more effective controls related to a method that is routinely used or over the integrity of data.

A52. When management makes extensive use of information technology in making an accounting estimate, controls relevant to the audit are likely to include general IT controls and application controls. Such controls may address risks related to:

- Whether the information technology system has the capability and is appropriately configured to process large volumes of data;
- Complex calculations in applying a method. When diverse systems are required to process complex transactions, regular reconciliations between the systems are made, in particular when the systems do not have automated interfaces or may be subject to manual intervention;
- Whether the design and calibration of models is periodically evaluated;
- The complete and accurate extraction of data regarding accounting estimates from the entity's records or from external information sources;
- Data, including the complete and accurate flow of data through the entity's information system, the appropriateness of any modification to the data used in making accounting estimates, the maintenance of the integrity and security of the data. When using external information sources, risks related to processing or recording the data;

- Whether management has controls around access, change and maintenance of individual models to maintain a strong audit trail of the accredited versions of models and to prevent unauthorized access or amendments to those models; and
 - Whether there are appropriate controls over the transfer of information relating to accounting estimates into the general ledger, including appropriate controls over journal entries.
- A53. In some industries, such as banking or insurance, the term governance may be used to describe activities within the control environment, monitoring of controls, and other components of internal control, as described in ISA 315 (Revised).³⁶
- A54. For entities with an internal audit function, its work may be particularly helpful to the auditor in obtaining an understanding of:
- The nature and extent of management's use of accounting estimates;
 - The design and implementation of control activities that address the risks related to the data, assumptions and models used to make the accounting estimates;
 - The aspects of the entity's information system that generate the data on which the accounting estimates are based; and
 - How new risks relating to accounting estimates are identified, assessed and managed.

Reviewing the Outcome or Re-Estimation of Previous Accounting Estimates (Ref: Para. 14)

- A55. A review of the outcome or re-estimation of previous accounting estimates (retrospective review) assists in identifying and assessing the risks of material misstatement when previous accounting estimates have an outcome through transfer or realization of the asset or liability in the current period, or are re-estimated for the purpose of the current period. Through performing a retrospective review, the auditor may obtain:
- Information regarding the effectiveness of management's previous estimation process, from which the auditor can obtain audit evidence about the likely effectiveness of management's current process
 - Audit evidence of matters, such as the reasons for changes that may be required to be disclosed in the financial statements.
 - Information regarding the complexity or estimation uncertainty pertaining to the accounting estimates.
 - Information regarding the susceptibility of accounting estimates to, or that may be an indicator of, possible management bias. The auditor's professional skepticism assists in identifying such circumstances or conditions and in determining the nature, timing and extent of further audit procedures.
- A56. A retrospective review may provide audit evidence that supports the identification and assessment of the risks of material misstatement in the current period. Such a retrospective review may be performed for accounting estimates made for the prior period's financial statements, or may be performed over several periods or a shorter period (such as half-yearly or quarterly). In some cases, a retrospective review over several periods may be appropriate when the outcome of an accounting estimate is resolved over a longer period.

³⁶ ISA 315 (Revised) paragraph A77

- A57. A retrospective review of management judgments and assumptions related to significant accounting estimates is required by ISA 240.³⁷ As a practical matter, the auditor's review of previous accounting estimates as a risk assessment procedure in accordance with this ISA may be carried out in conjunction with the review required by ISA 240.
- A58. Based on the auditor's previous assessment of the risks of material misstatement, for example, if inherent risk is assessed as higher for one or more risks of material misstatement, the auditor may judge that a more detailed retrospective review is required. As part of the detailed retrospective review, the auditor may pay particular attention, when practicable, to the effect of data and significant assumptions used in making the previous accounting estimates. On the other hand, for example, for accounting estimates that arise from the recording of routine and recurring transactions, the auditor may judge that the application of analytical procedures as risk assessment procedures is sufficient for purposes of the review.
- A59. The measurement objective for fair value accounting estimates and other accounting estimates, based on current conditions at the measurement date, deals with perceptions about value at a point in time, which may change significantly and rapidly as the environment in which the entity operates changes. The auditor may therefore focus the review on obtaining information that may be relevant to identifying and assessing risks of material misstatement. For example, in some cases, obtaining an understanding of changes in marketplace participant assumptions that affected the outcome of a previous period's fair value accounting estimates may be unlikely to provide relevant audit evidence. In this case, audit evidence may be obtained by understanding the outcomes of assumptions (such as a cash flow projections) and understanding the effectiveness of management's prior estimation process that supports the identification and assessment of the risk of material misstatement in the current period.
- A60. A difference between the outcome of an accounting estimate and the amount recognized in the previous period's financial statements does not necessarily represent a misstatement of the previous period's financial statements. However, such a difference may represent a misstatement if, for example, the difference arises from information that was available to management when the previous period's financial statements were finalized, or that could reasonably be expected to have been obtained and taken into account in the context of the applicable financial reporting framework.³⁸ Such a difference may call into question management's process for taking information into account in making the accounting estimate. As a result, the auditor may reassess control risk and may determine that more persuasive audit evidence needs to be obtained about the matter. Many financial reporting frameworks contain guidance on distinguishing between changes in accounting estimates that constitute misstatements and changes that do not, and the accounting treatment required to be followed in each case.

Specialized Skills or Knowledge (Ref: Para. 15)

- A61. Matters that may affect the auditor's determination of whether the engagement team requires specialized skills or knowledge, include, for example:³⁹
- The nature of the accounting estimates for a particular business or industry (for example, mineral deposits, agricultural assets, complex financial instruments, insurance contract liabilities).

³⁷ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraph 32(b)(ii)

³⁸ ISA 560, *Subsequent Events*, paragraph 14

³⁹ ISA 220, *Quality Control for an Audit of Financial Statements*, paragraph 14 and ISA 300, *Planning an Audit of Financial Statements*, paragraph 8(e)

- The degree of estimation uncertainty.
- The complexity of the method or model used.
- The complexity of the requirements of the applicable financial reporting framework relevant to accounting estimates, including whether there are areas known to be subject to differing interpretation or practice or areas where there are inconsistencies in how accounting estimates are made.
- The procedures the auditor intends to undertake in responding to assessed risks of material misstatement.
- The need for judgment about matters not specified by the applicable financial reporting framework.
- The degree of judgment needed to select data and assumptions.
- The complexity and extent of the entity's use of information technology in making accounting estimates.

The nature, timing and extent of the involvement of individuals with specialized skills and knowledge may vary throughout the audit.

- A62. The auditor may not possess the specialized skills or knowledge necessary when the matter involved is in a field other than accounting or auditing (for example, valuation skills) and may need to use an auditor's expert.⁴⁰
- A63. Many accounting estimates do not require the application of specialized skills or knowledge. For example, specialized skills or knowledge may not be needed for a simple inventory obsolescence calculation. However, for example, for expected credit losses of a banking institution or an insurance contract liability for an insurance entity, the auditor is likely to conclude that it is necessary to apply specialized skills or knowledge.

Identifying and Assessing the Risks of Material Misstatement (Ref: Para. 4, 16)

- A64. Identifying and assessing risks of material misstatement at the assertion level relating to accounting estimates is important for all accounting estimates, including not only those that are recognized in the financial statements, but also those that are included in the notes to the financial statements.
- A65. Paragraph A42 of ISA 200 states that the ISAs do not ordinarily refer to inherent risk and control risk separately. However, this ISA requires a separate assessment of inherent risk and control risk to provide a basis for designing and performing further audit procedures to respond to the risks of material misstatement, including significant risks, at the assertion level for accounting estimates in accordance with ISA 330.⁴¹
- A66. In identifying the risks of material misstatement and in assessing inherent risk, the auditor is required to take into account the degree to which the accounting estimate is subject to, or affected by, estimation uncertainty, complexity, subjectivity, or other inherent risk factors. The auditor's consideration of the inherent risk factors may also provide information to be used in determining:
- Where inherent risk is assessed on the spectrum of inherent risk; and

⁴⁰ ISA 620, *Using the Work of an Auditor's Expert*

⁴¹ ISA 330, paragraph 7(b)

- The reasons for the assessment given to the risks of material misstatement at the assertion level, and that the auditor's further audit procedures in accordance with paragraph 18 are responsive to those reasons.

The interrelationships between the inherent risk factors are further explained in Appendix 1.

A67. The reasons for the auditor's assessment of inherent risk at the assertion level may result from one or more of the inherent risk factors of estimation uncertainty, complexity, subjectivity or other inherent risk factors. For example:

- (a) Accounting estimates of expected credit losses are likely to be complex because the expected credit losses cannot be directly observed and may require the use of a complex model. The model may use a complex set of historical data and assumptions about future developments in a variety of entity specific scenarios that may be difficult to predict. Accounting estimates for expected credit losses are also likely to be subject to high estimation uncertainty and significant subjectivity in making judgments about future events or conditions. Similar considerations apply to insurance contract liabilities.
- (b) An accounting estimate for an obsolescence provision for an entity with a wide range of different inventory types may require complex systems and processes, but may involve little subjectivity and the degree of estimation uncertainty may be low, depending on the nature of the inventory.
- (c) Other accounting estimates may not be complex to make but may have high estimation uncertainty and require significant judgment, for example, an accounting estimate that requires a single critical judgment about a liability, the amount of which is contingent on the outcome of the litigation.

A68. The relevance and significance of inherent risk factors may vary from one estimate to another. Accordingly, the inherent risk factors may, either individually or in combination, affect simple accounting estimates to a lesser degree and the auditor may identify fewer risks or assess inherent risk at the lower end of the spectrum of inherent risk.

A69. Conversely, the inherent risk factors may, either individually or in combination, affect complex accounting estimates to a greater degree, and may lead the auditor to assess inherent risk at the higher end of the spectrum of inherent risk. For these accounting estimates, the auditor's consideration of the effects of the inherent risk factors is likely to directly affect the number and nature of identified risks of material misstatement, the assessment of such risks, and ultimately the persuasiveness of the audit evidence needed in responding to the assessed risks. Also, for these accounting estimates the auditor's application of professional skepticism may be particularly important.

A70. Events occurring after the date of the financial statements may provide additional information relevant to the auditor's assessment of the risks of material misstatement at the assertion level. For example, the outcome of an accounting estimate may become known during the audit. In such cases, the auditor may assess or revise the assessment of the risks of material misstatement at the assertion level,⁴² regardless of the degree to which the accounting estimate was subject to, or affected by estimation uncertainty, complexity, subjectivity or other inherent risk factors. Events occurring after the date of the financial statements also may influence the auditor's selection of the approach to testing the accounting estimate in accordance with paragraph 18. For example, for a simple bonus accrual that is based on a straightforward percentage of compensation for selected employees, the auditor may conclude that there is

⁴² ISA 315 (Revised), paragraph 31

relatively little complexity or subjectivity in making the accounting estimate, and therefore may assess inherent risk at the assertion level at the lower end of the spectrum of inherent risk. The payment of the bonuses subsequent to period end may provide sufficient appropriate audit evidence regarding the assessed risks of material misstatement at the assertion level.

- A71. The auditor's assessment of control risk may be done in different ways depending on preferred audit techniques or methodologies. The control risk assessment may be expressed using qualitative categories (for example, control risk assessed as maximum, moderate, minimum) or in terms of the auditor's expectation of how effective the control(s) is in addressing the identified risk, that is, the planned reliance on the effective operation of controls. For example, if control risk is assessed as maximum, the auditor contemplates no reliance on the effective operation of controls. If control risk is assessed at less than maximum, the auditor contemplates reliance on the effective operation of controls.

Estimation Uncertainty (Ref: Para. 16(a))

- A72. In taking into account the degree to which the accounting estimate is subject to estimation uncertainty, the auditor may consider:

- Whether the applicable financial reporting framework requires:
 - The use of a method to make the accounting estimate that inherently has a high level of estimation uncertainty. For example, the financial reporting framework may require the use of unobservable inputs.
 - The use of assumptions that inherently have a high level of estimation uncertainty, such as assumptions with a long forecast period, assumptions that are based on data that is unobservable and are therefore difficult for management to develop, or the use of various assumptions that are interrelated.
 - Disclosures about estimation uncertainty.
- The business environment. An entity may be active in a market that experiences turmoil or possible disruption (for example, from major currency movements or inactive markets) and the accounting estimate may therefore be dependent on data that is not readily observable.
- Whether it is possible (or practicable, insofar as permitted by the applicable financial reporting framework) for management:
 - To make a precise and reliable prediction about the future realization of a past transaction (for example, the amount that will be paid under a contingent contractual term), or about the incidence and impact of future events or conditions (for example, the amount of a future credit loss or the amount at which an insurance claim will be settled and the timing of its settlement); or
 - To obtain precise and complete information about a present condition (for example, information about valuation attributes that would reflect the perspective of market participants at the date of the financial statements, to develop a fair value estimate).

- A73. The size of the amount recognized or disclosed in the financial statements for an accounting estimate is not, in itself, an indicator of its susceptibility to misstatement because, for example, the accounting estimate may be understated.

- A74. In some circumstances, the estimation uncertainty may be so high that a reasonable accounting estimate cannot be made. The applicable financial reporting framework may preclude recognition of an item in the financial statements, or its measurement at fair value. In such cases, there may

be risks of material misstatement that relate not only to whether an accounting estimate should be recognized, or whether it should be measured at fair value, but also to the reasonableness of the disclosures. With respect to such accounting estimates, the applicable financial reporting framework may require disclosure of the accounting estimates and the estimation uncertainty associated with them (see paragraphs A112–A113, A143–A144).

- A75. In some cases, the estimation uncertainty relating to an accounting estimate may cast significant doubt about the entity's ability to continue as a going concern. ISA 570 (Revised)⁴³ establishes requirements and provides guidance in such circumstances.

Complexity or Subjectivity (Ref: Para. 16(b))

The Degree to Which Complexity Affects the Selection and Application of the Method

- A76. In taking into account the degree to which the selection and application of the method used in making the accounting estimate are affected by complexity, the auditor may consider:

- The need for specialized skills or knowledge by management which may indicate that the method used to make an accounting estimate is inherently complex and therefore the accounting estimate may have a greater susceptibility to material misstatement. There may be a greater susceptibility to material misstatement when management has developed a model internally and has relatively little experience in doing so, or uses a model that applies a method that is not established or commonly used in a particular industry or environment.
- The nature of the measurement basis required by the applicable financial reporting framework, which may result in the need for a complex method that requires multiple sources of historical and forward-looking data or assumptions, with multiple interrelationships between them. For example, an expected credit loss provision may require judgments about future credit repayments and other cash flows, based on consideration of historical experience data and the application of forward looking assumptions. Similarly, the valuation of an insurance contract liability may require judgments about future insurance contract payments to be projected based on historical experience and current and assumed future trends.

The Degree to Which Complexity Affects the Selection and Application of the Data

- A77. In taking into account the degree to which the selection and application of the data used in making the accounting estimate are affected by complexity, the auditor may consider:

- The complexity of the process to derive the data, taking into account the relevance and reliability of the data source. Data from certain sources may be more reliable than from others. Also, for confidentiality or proprietary reasons, some external information sources will not (or not fully) disclose information that may be relevant in considering the reliability of the data they provide, such as the sources of the underlying data they used or how it was accumulated and processed.
- The inherent complexity in maintaining the integrity of the data. When there is a high volume of data and multiple sources of data, there may be inherent complexity in maintaining the integrity of data that is used to make an accounting estimate.
- The need to interpret complex contractual terms. For example, the determination of cash inflows or outflows arising from a commercial supplier or customer rebates may depend on

⁴³ ISA 570, (Revised), *Going Concern*

very complex contractual terms that require specific experience or competence to understand or interpret.

The Degree to Which Subjectivity Affects the Selection and Application of the Method, Assumptions or Data

A78. In taking into account the degree to which the selection and application of method, assumptions or data are affected by subjectivity, the auditor may consider:

- The degree to which the applicable financial reporting framework does not specify the valuation approaches, concepts, techniques and factors to use in the estimation method.
- The uncertainty regarding the amount or timing, including the length of the forecast period. The amount and timing is a source of inherent estimation uncertainty, and gives rise to the need for management judgment in selecting a point estimate, which in turn creates an opportunity for management bias. For example, an accounting estimate that incorporates forward looking assumptions may have a high degree of subjectivity which may be susceptible to management bias.

Other Inherent Risk Factors (Ref: Para. 16(b))

A79. The degree of subjectivity associated with an accounting estimate influences the susceptibility of the accounting estimate to misstatement due to management bias or fraud. For example, when an accounting estimate is subject to a high degree of subjectivity, the accounting estimate is likely to be more susceptible to misstatement due to management bias or fraud and this may result in a wide range of possible measurement outcomes. Management may select a point estimate from that range that is inappropriate in the circumstances, or that is inappropriately influenced by unintentional or intentional management bias, and that is therefore misstated. For continuing audits, indicators of possible management bias identified during the audit of preceding periods may influence the planning and risk assessment procedures in the current period.

Significant Risks (Ref: Para. 17)

A80. The auditor's assessment of inherent risk, which takes into account the degree to which an accounting estimate is subject to, or affected by estimation uncertainty, complexity, subjectivity or other inherent risk factors, assists the auditor in determining whether any of the risks of material misstatement identified and assessed are a significant risk.

Responses to the Assessed Risks of Material Misstatement

The Auditor's Further Audit Procedures (Ref: Para. 18)

A81. In designing and performing further audit procedures the auditor may use any of the three testing approaches (individually or in combination) listed in paragraph 18. For example, when several assumptions are used to make an accounting estimate, the auditor may decide to use a different testing approach for each assumption tested.

Obtaining Relevant Audit Evidence Whether Corroborative or Contradictory

A82. Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions.⁴⁴ Obtaining audit evidence in an unbiased manner may involve obtaining evidence from multiple sources within and outside

⁴⁴ ISA 500, paragraph A1

the entity. However, the auditor is not required to perform an exhaustive search to identify all possible sources of audit evidence.

- A83. ISA 330 requires the auditor to obtain more persuasive audit evidence the higher the auditor's assessment of the risk.⁴⁵ Therefore, the consideration of the nature or quantity of the audit evidence may be more important when inherent risks relating to an accounting estimate is assessed at the higher end of the spectrum of inherent risk.

Scalability

- A84. The nature, timing and extent of the auditor's further audit procedures are affected by, for example:

- The assessed risks of material misstatement, which affect the persuasiveness of the audit evidence needed and influence the approach the auditor selects to audit an accounting estimate. For example, the assessed risks of material misstatement relating to the existence or valuation assertions may be lower for a straightforward accrual for bonuses that are paid to employees shortly after period end. In this situation, it may be more practical for the auditor to obtain sufficient appropriate audit evidence by evaluating events occurring up to the date of the auditor's report, rather than through other testing approaches.
- The reasons for the assessed risks of material misstatement.

When the Auditor Intends to Rely on the Operating Effectiveness of Relevant Controls (Ref: Para: 19)

- A85. Testing the operating effectiveness of relevant controls may be appropriate when inherent risk is assessed as higher on the spectrum of inherent risk, including for significant risks. This may be the case when the accounting estimate is subject to or affected by a high degree of complexity. When the accounting estimate is affected by a high degree of subjectivity, and therefore requires significant judgment by management, inherent limitations in the effectiveness of the design of controls may lead the auditor to focus more on substantive procedures than on testing the operating effectiveness of controls.

- A86. In determining the nature, timing and extent of testing of the operating effectiveness of controls relating to accounting estimates, the auditor may consider factors such as:

- The nature, frequency and volume of transactions;
- The effectiveness of the design of the controls, including whether controls are appropriately designed to respond to the assessed inherent risk, and the strength of governance;
- The importance of particular controls to the overall control objectives and processes in place at the entity, including the sophistication of the information system to support transactions;
- The monitoring of controls and identified deficiencies in internal control;
- The nature of the risks the controls are intended to address, for example, controls related to the exercise of judgment compared with controls over supporting data;
- The competency of those involved in the control activities;
- The frequency of performance of the control activities; and
- The evidence of performance of control activities.

⁴⁵ ISA 330, paragraph 7(b), A19

Substantive Procedures Alone Cannot Provide Sufficient Appropriate Audit Evidence

A87. In some industries, such as the financial services industry, management makes extensive use of IT to conduct business. It may therefore be more likely that there are risks related to certain accounting estimates for which substantive procedures alone cannot provide sufficient appropriate audit evidence.

A88. Circumstances when risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level may exist include:

- When controls are necessary to mitigate risks relating to the initiation, recording, processing, or reporting of information obtained from outside of the general and subsidiary ledgers.
- Information supporting one or more assertions is electronically initiated, recorded, processed, or reported. This is likely to be the case when there is a high volume of transactions or data, or a complex model is used, requiring the extensive use of information technology to ensure the accuracy and completeness of the information. A complex expected credit loss provision may be required for a financial institution or utility entity. For example, in the case of a utility entity, the data used in developing the expected credit loss provision may comprise many small balances resulting from a high volume of transactions. In these circumstances, the auditor may conclude that sufficient appropriate audit evidence cannot be obtained without testing controls around the model used to develop the expected credit loss provision.

In such cases, the sufficiency and appropriateness of the audit evidence may depend on the effectiveness of controls over the accuracy and completeness of the information.

A89. As part of the audit of the financial statements for certain entities (such as a bank or insurer), the auditor also may be required by law or regulation to undertake additional procedures in relation to, or to provide an assurance conclusion on, internal control. In these and other similar circumstances, the auditor may be able to use information obtained in performing such procedures as audit evidence, subject to determining whether subsequent changes have occurred that may affect its relevance to the audit.

Significant Risks (Ref: Para. 20)

A90. When the auditor's further audit procedures in response to a significant risk consist only of substantive procedures, ISA 330⁴⁶ requires that those procedures include tests of details. Such tests of details may be designed and performed under each of the approaches described in paragraph 18 of this ISA based on the auditor's professional judgment in the circumstances. Examples of tests of details for significant risks related to accounting estimates include:

- Examination, for example, examining contracts to corroborate terms or assumptions.
- Recalculation, for example, verifying the mathematical accuracy of a model.
- Agreeing assumptions used to supporting documentation, such as third-party published information.

Obtaining Audit Evidence from Events Occurring up to the Date of the Auditor's Report (Ref: Para. 21)

A91. In some circumstances, obtaining audit evidence from events occurring up to the date of the auditor's report may provide sufficient appropriate audit evidence to address the risks of material

⁴⁶ ISA 330, paragraph 21

misstatement. For example, sale of the complete inventory of a discontinued product shortly after the period end may provide sufficient appropriate audit evidence relating to the estimate of its net realizable value at the period end. In other cases, it may be necessary to use this testing approach in connection with another approach in paragraph 18.

- A92. For some accounting estimates, events occurring up to the date of the auditor's report are unlikely to provide sufficient appropriate audit evidence regarding the accounting estimate. For example, the conditions or events relating to some accounting estimates develop only over an extended period. Also, because of the measurement objective of fair value accounting estimates, information after the period-end may not reflect the events or conditions existing at the balance sheet date and therefore may not be relevant to the measurement of the fair value accounting estimate.
- A93. Even if the auditor decides not to undertake this testing approach in respect of specific accounting estimates, the auditor is required to comply with ISA 560. ISA 560 requires the auditor to perform audit procedures designed to obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements have been identified⁴⁷ and appropriately reflected in the financial statements.⁴⁸ Because the measurement of many accounting estimates, other than fair value accounting estimates, usually depends on the outcome of future conditions, transactions or events, the auditor's work under ISA 560 is particularly relevant.

Testing How Management Made the Accounting Estimate (Ref. Para. 22)

- A94. Testing how management made the accounting estimate may be an appropriate approach when, for example:
- The auditor's review of similar accounting estimates made in the prior period financial statements suggests that management's current period process is appropriate.
 - The accounting estimate is based on a large population of items of a similar nature that individually are not significant.
 - The applicable financial reporting framework specifies how management is expected to make the accounting estimate. For example, this may be the case for an expected credit loss provision.
 - The accounting estimate is derived from the routine processing of data.

Testing how management made the accounting estimate may also be an appropriate approach when neither of the other testing approaches is practical to perform, or may be an appropriate approach in combination with one of the other testing approaches.

Changes in Methods, Significant Assumptions and the Data from Prior Periods (Ref: Para. 23(a), 24(a), 25(a))

- A95. When a change from prior periods in a method, significant assumption, or the data is not based on new circumstances or new information, or when significant assumptions are inconsistent with each other and with those used in other accounting estimates, or with related assumptions used in other areas of the entity's business activities, the auditor may need to have further discussions

⁴⁷ ISA 560, paragraph 6

⁴⁸ ISA 560, paragraph 8

with management about the circumstances and, in doing so, challenge management regarding the appropriateness of the assumptions used.

Indicators of Management Bias (Ref: Para. 23(b), 24(b), 25(b))

A96. When the auditor identifies indicators of possible management bias, the auditor may need a further discussion with management and may need to reconsider whether sufficient appropriate audit evidence has been obtained that the method, assumptions and data used were appropriate and supportable in the circumstances. An example of an indicator of management bias for a particular accounting estimate may be when management has developed an appropriate range for several different assumptions, and in each case the assumption used was from the end of the range that resulted in the most favorable measurement outcome.

Methods

The selection of the method (Ref: Para. 23(a))

A97. Relevant considerations for the auditor regarding the appropriateness of the method selected in the context of the applicable financial reporting framework, and, if applicable, the appropriateness of changes from the prior period may include:

- Whether management's rationale for the method selected is appropriate;
- Whether the method is appropriate in the circumstances given the nature of the accounting estimate, the requirements of the applicable financial reporting framework, other available valuation concepts or techniques, regulatory requirements, and the business, industry and environment in which the entity operates;
- When management has determined that different methods result in a range of significantly different estimates, how management has investigated the reasons for these differences; and
- Whether the change is based on new circumstances or new information. When this is not the case, the change may not be reasonable or in compliance with the applicable financial reporting framework. Arbitrary changes result in inconsistent financial statements over time and may give rise to financial statement misstatements or may be an indicator of possible management bias. (see also paragraphs A133–A136)

These matters are important when the applicable financial reporting framework does not prescribe the method of measurement or allows multiple methods.

Complex modelling (Ref: Para. 23(d))

A98. A model, and the related method, is more likely to be complex when:

- Understanding and applying the method, including designing the model and selecting and using appropriate data and assumptions, requires specialized skills or knowledge;
- It is difficult to obtain data needed for use in the model because there are restrictions on the availability or observability of, or access to, data; or
- It is difficult to maintain the integrity (e.g., accuracy, consistency, or completeness) of the data and assumptions in using the model due to multiple valuation attributes, multiple relationships between them, or multiple iterations of the calculation.

A99. Matters that the auditor may consider when management uses a complex model include, for example, whether:

- The model is validated prior to usage or when there has been a change to the model, with periodic reviews to ensure it is still suitable for its intended use. The entity's validation process may include evaluation of:
 - The model's theoretical soundness;
 - The model's mathematical integrity;
 - The accuracy and completeness of the model's data and assumptions; and
 - The model's output as compared to actual transactions.
- Appropriate change control policies and procedures exist.
- Management uses appropriate skills and knowledge in using the model.

These considerations may also be useful for a method that does not involve complex modelling.

A100. Management may make adjustments to the output of the model to meet the requirements of the applicable financial reporting framework. In some industries these adjustments are referred to as overlays. In the case of fair value accounting estimates, it may be relevant to consider whether adjustments to the output of the model, if any, reflect the assumptions marketplace participants would use in similar circumstances.

Maintenance of integrity of significant assumptions and the data used in applying the method (Ref: Para. 23(e))

A101. Maintaining the integrity of significant assumptions and the data in applying the method refers to the maintenance of the accuracy and completeness of the data and assumptions through all stages of information processing. A failure to maintain such integrity may result in corruption of the data and assumptions and may give rise to misstatements. In this regard, relevant considerations for the auditor may include whether the data and assumptions are subject to all changes intended by management, and not subject to any unintended changes, during activities such as input, storage, retrieval, transmission or processing.

Significant Assumptions (Ref: Para. 24)

A102. Relevant considerations for the auditor regarding the appropriateness of the significant assumptions in the context of the applicable financial reporting framework, and, if applicable, the appropriateness of changes from the prior period may include:

- Management's rationale for the selection of the assumption;
- Whether the assumption is appropriate in the circumstances given the nature of the accounting estimate, the requirements of the applicable financial reporting framework, and the business, industry and environment in which the entity operates; and
- Whether a change from prior periods in selecting an assumption is based on new circumstances or new information. When it is not, the change may not be reasonable nor in compliance with the applicable financial reporting framework. Arbitrary changes in an accounting estimate may give rise to material misstatements of the financial statements or may be an indicator of possible management bias (see paragraphs A133–A136).

A103. Management may evaluate alternative assumptions or outcomes of accounting estimates, which may be accomplished through a number of approaches depending on the circumstances. One possible approach is a sensitivity analysis. This might involve determining how the monetary amount of an accounting estimate varies with different assumptions. Even for accounting

estimates measured at fair value, there may be variation because different market participants will use different assumptions. A sensitivity analysis may lead to the development of a number of outcome scenarios, sometimes characterized as a range of outcomes by management, and including 'pessimistic' and 'optimistic' scenarios.

A104. Through the knowledge obtained in performing the audit, the auditor may become aware of or may have obtained an understanding of assumptions used in other areas of the entity's business. Such matters may include, for example, business prospects, assumptions in strategy documents and future cash flows. Also, if the engagement partner has performed other engagements for the entity, ISA 315 (Revised)⁴⁹ requires the engagement partner to consider whether information obtained from those other engagements is relevant to identifying risks of material misstatement. This information may also be useful to consider in addressing whether significant assumptions are consistent with each other and with those used in other accounting estimates.

A105. The appropriateness of the significant assumptions in the context of the requirements of the applicable financial reporting framework may depend on management's intent and ability to carry out certain courses of action. Management often documents plans and intentions relevant to specific assets or liabilities and the applicable financial reporting framework may require management to do so. The nature and extent of audit evidence to be obtained about management's intent and ability is a matter of professional judgment. When applicable, the auditor's procedures may include the following:

- Review of management's history of carrying out its stated intentions.
- Inspection of written plans and other documentation, including, when applicable, formally approved budgets, authorizations or minutes.
- Inquiry of management about its reasons for a particular course of action.
- Review of events occurring subsequent to the date of the financial statements and up to the date of the auditor's report.
- Evaluation of the entity's ability to carry out a particular course of action given the entity's economic circumstances, including the implications of its existing commitments and legal, regulatory, or contractual restrictions that could affect the feasibility of management's actions.
- Consideration of whether management has met the applicable documentation requirements, if any, of the applicable financial reporting framework.

Certain financial reporting frameworks, however, may not permit management's intentions or plans to be taken into account when making an accounting estimate. This is often the case for fair value accounting estimates because their measurement objective requires that significant assumptions reflect those used by marketplace participants.

Data (Ref: Para. 25(a))

A106. Relevant considerations for the auditor regarding the appropriateness of the data selected for use in the context of the applicable financial reporting framework, and, if applicable, the appropriateness of the changes from the prior period may include:

- Management's rationale for the selection of the data;

⁴⁹ ISA 315 (Revised), paragraph 8

- Whether the data is appropriate in the circumstances given the nature of the accounting estimate, the requirements of the applicable financial reporting framework, and the business, industry and environment in which the entity operates; and
- Whether the change from prior periods in the sources or items of data selected or data selected, is based on new circumstances or new information. When it is not, it is unlikely to be reasonable nor in compliance with the applicable financial reporting framework. Arbitrary changes in an accounting estimate result in inconsistent financial statements over time and may give rise to financial statement misstatements or may be an indicator of possible management bias (see paragraphs A133–A136).

Relevance and reliability of the data (Ref: Para. 25(c))

A107. When using information produced by the entity, ISA 500 requires the auditor to evaluate whether the information is sufficiently reliable for the auditor's purposes, including as necessary in the circumstances, to obtain audit evidence about the accuracy and completeness of the information and evaluating whether the information is sufficiently precise and detailed for the auditor's purposes.⁵⁰

Complex legal or contractual terms (Ref: Para. 25(d))

A108. Procedures that the auditor may consider when the accounting estimate is based on complex legal or contractual terms include:

- Considering whether specialized skills or knowledge are needed to understand or interpret the contract;
- Inquiring of the entity's legal counsel regarding the legal or contractual terms; and
- Inspecting the underlying contracts to:
 - Evaluate, the underlying business purpose for the transaction or agreement; and
 - Consider whether the terms of the contracts are consistent with management's explanations.

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

Management's steps to understand and address estimation uncertainty (Ref: Para. 26(a))

A109. Relevant considerations regarding whether management has taken appropriate steps to understand and address estimation uncertainty may include whether management has:

- (a) Understood the estimation uncertainty, through identifying the sources, and assessing the degree of inherent variability in the measurement outcomes and the resulting range of reasonably possible measurement outcomes;
- (b) Identified the degree to which, in the measurement process, complexity or subjectivity affect the risk of material misstatement, and addressed the resulting potential for misstatement through applying:
 - (i) Appropriate skills and knowledge in making accounting estimates; and
 - (ii) Professional judgment, including by identifying and addressing susceptibility to management bias; and

⁵⁰ ISA 500, paragraph 9

- (c) Addressed estimation uncertainty through appropriately selecting management's point estimate and related disclosures that describe the estimation uncertainty.

The selection of management's point estimate and related disclosures of estimation uncertainty (Ref: Para. 26(b))

A110. Matters that may be relevant regarding the selection of management's point estimate and the development of related disclosures about estimation uncertainty include whether:

- The methods and data used were selected appropriately, including when alternative methods for making the accounting estimate and alternative sources of data were available.
- Valuation attributes used were appropriate and complete.
- The assumptions used were selected from a range of reasonably possible amounts and were supported by appropriate data that is relevant and reliable.
- The data used was appropriate, relevant and reliable, and the integrity of that data was maintained.
- The calculations were applied in accordance with the method and were mathematically accurate.
- Management's point estimate is appropriately chosen from the reasonably possible measurement outcomes.
- The related disclosures appropriately describe the amount as an estimate and explain the nature and limitations of the estimation process, including the variability of the reasonably possible measurement outcomes.

A111. Relevant considerations for the auditor regarding the appropriateness of management's point estimate, may include:

- When the requirements of the applicable financial reporting framework prescribe the point estimate that is to be used after consideration of the alternative outcomes and assumptions, or prescribes a specific measurement method, whether management has followed the requirements of the applicable financial reporting framework.
- When the applicable financial reporting framework has not specified how to select an amount from reasonably possible measurement outcomes, whether management has exercised judgment, taking into account the requirements of the applicable financial reporting framework.

A112. Relevant considerations for the auditor regarding management's disclosures about estimation uncertainty include the requirements of the applicable financial reporting framework, which may require disclosures:

- That describe the amount as an estimate and explain the nature and limitations of the process for making it, including the variability in reasonably possible measurement outcomes. The framework also may require additional disclosures to meet a disclosure objective.⁵¹
- About significant accounting policies related to accounting estimates. Depending on the circumstances, relevant accounting policies may include matters such as the specific

⁵¹ IFRS 13, *Fair Value Measurement*, paragraph 92

principles, bases, conventions, rules and practices applied in preparing and presenting accounting estimates in the financial statements.

- About significant or critical judgments (for example, those that had the most significant effect on the amounts recognized in the financial statements) as well as significant forward-looking assumptions or other sources of estimation uncertainty.

In certain circumstances, additional disclosures beyond those explicitly required by the financial reporting framework may be needed in order to achieve fair presentation, or in the case of a compliance framework, for the financial statements not to be misleading.

A113. The greater the degree to which an accounting estimate is subject to estimation uncertainty, the more likely the risks of material misstatement will be assessed as higher and therefore the more persuasive the audit evidence needs to be to determine, in accordance with paragraph 35, whether management's point estimate and related disclosures about estimation uncertainty are reasonable in the context of the applicable financial reporting framework, or are misstated.

A114. If the auditor's consideration of estimation uncertainty associated with an accounting estimate, and its related disclosure, is a matter that required significant auditor attention, then this may constitute a key audit matter.⁵²

When Management Has Not Taken Appropriate Steps to Understand and Address Estimation Uncertainty (Ref: Para. 27)

A115. When the auditor determines that management has not taken appropriate steps to understand and address estimation uncertainty, additional procedures that the auditor may request management to perform to understand estimation uncertainty may include, for example, consideration of alternative assumptions or the performance of a sensitivity analysis.

A116. In considering whether it is practicable to develop a point estimate or range, matters the auditor may need to take into account include whether the auditor could do so without compromising independence requirements. This may include relevant ethical requirements that address prohibitions on assuming management responsibilities.

A117. If, after considering management's response, the auditor determines that it is not practicable to develop an auditor's point estimate or range, the auditor is required to evaluate the implications for the audit or the auditor's opinion on the financial statements in accordance with paragraph 34.

Developing an Auditor's Point Estimate or Using an Auditor's Range (Ref: Para. 28–29)

A118. Developing an auditor's point estimate or range to evaluate management's point estimate and related disclosures about estimation uncertainty may be an appropriate approach when, for example:

- The auditor's review of similar accounting estimates made in the prior period financial statements suggests that management's current period process is not expected to be effective.
- The entity's controls within and over management's process for making accounting estimates are not well designed or properly implemented.
- Events or transactions between the period end and the date of the auditor's report have not been properly taken into account, when it is appropriate for management to do so, and such events or transactions appear to contradict management's point estimate.

⁵² ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

- There are appropriate alternative assumptions or sources of relevant data that can be used in developing an auditor's point estimate or a range.
- Management has not taken appropriate steps to understand or address the estimation uncertainty (see paragraph 27).

A119. The decision to develop a point estimate or range also may be influenced by the applicable financial reporting framework, which may prescribe the point estimate that is to be used after consideration of the alternative outcomes and assumptions, or prescribe a specific measurement method (for example, the use of a discounted probability-weighted expected value, or the most likely outcome).

A120. The auditor's decision as to whether to develop a point estimate rather than a range may depend on the nature of the estimate and the auditor's judgment in the circumstances. For example, the nature of the estimate may be such that there is expected to be less variability in the reasonably possible outcomes. In these circumstances, developing a point estimate may be an effective approach, particularly when it can be developed with a higher degree of precision.

A121. The auditor may develop a point estimate or a range in a number of ways, for example, by:

- Using a different model than the one used by management, for example, one that is commercially available for use in a particular sector or industry, or a proprietary or auditor-developed model.
- Using management's model but developing alternative assumptions or data sources to those used by management.
- Using the auditor's own method but developing alternative assumptions to those used by management.
- Employing or engaging a person with specialized expertise to develop or execute a model, or to provide relevant assumptions.
- Consideration of other comparable conditions, transactions or events, or, where relevant, markets for comparable assets or liabilities.

A122. The auditor also may develop a point estimate or range for only part of the accounting estimate (for example, for a particular assumption, or when only a certain part of the accounting estimate is giving rise to the risk of material misstatement).

A123. When using the auditor's own methods, assumptions or data to develop a point estimate or range, the auditor may obtain evidence about the appropriateness of management's methods, assumptions or data. For example, if the auditor uses the auditor's own assumptions in developing a range to evaluate the reasonableness of management's point estimate, the auditor may also develop a view about whether management's judgments in selecting the significant assumptions used in making the accounting estimate give rise to indicators of possible management bias.

A124. The requirement in paragraph 29(a) for the auditor to determine that the range includes only amounts that are supported by sufficient appropriate audit evidence does not mean that the auditor is expected to obtain audit evidence to support each possible outcome in the range individually. Rather, the auditor is likely to obtain evidence to determine that the points at both ends of the range are reasonable in the circumstances, thereby supporting that amounts falling between those two points also are reasonable.

A125. The size of the auditor's range may be multiples of materiality for the financial statements as a whole, particularly when materiality is based on operating results (for example, pre-tax income) and this measure is relatively small in relation to assets or other balance sheet measures. This situation is more likely to arise in circumstances when the estimation uncertainty associated with the accounting estimate is itself multiples of materiality, which is more common for certain types of accounting estimates or in certain industries, such as insurance or banking, where a high degree of estimation uncertainty is more typical and there may be specific requirements in the applicable financial reporting framework in that regard. Based on the procedures performed and audit evidence obtained in accordance with the requirements of this ISA, the auditor may conclude that a range that is multiples of materiality is, in the auditor's judgment, appropriate in the circumstances. When this is the case, the auditor's evaluation of the reasonableness of the disclosures about estimation uncertainty becomes increasingly important, particularly whether such disclosures appropriately convey the high degree of estimation uncertainty and the range of possible outcomes. Paragraphs A139–A144 include additional considerations that may be relevant in these circumstances.

Other Considerations Relating to Audit Evidence (Ref: Para. 30)

A126. Information to be used as audit evidence, regarding risks of material misstatement relating to accounting estimates, may have been produced by the entity, prepared using the work of a management's expert, or provided by an external information source.

External Information Sources

A127. As explained in ISA 500,⁵³ the reliability of information from an external information source is influenced by its source, its nature, and the circumstances under which it is obtained. Consequently, the nature and extent of the auditor's further audit procedures to consider the reliability of the information used in making an accounting estimate may vary depending on the nature of these factors. For example:

- When market or industry data, prices, or pricing related data, are obtained from a single external information source, specializing in such information, the auditor may seek a price from an alternative independent source with which to compare.
- When market or industry data, prices, or pricing related data, are obtained from multiple independent external information sources and points to consensus across those sources, the auditor may need to obtain less evidence about the reliability of the data from an individual source.
- When information obtained from multiple information sources points to divergent market views the auditor may seek to understand the reasons for the diversity in views. The diversity may result from the use of different methods, assumptions, or data. For example, one source may be using current prices and another source using future prices. When the diversity relates to estimation uncertainty, the auditor is required by paragraph 26(b) to obtain sufficient appropriate audit evidence about whether, in the context of the applicable financial reporting framework, the disclosures in the financial statements that describe the estimation uncertainty are reasonable. In such cases professional judgment is also important in considering information about the methods, assumptions or data applied.
- When information obtained from an external information source has been developed by that source using its own model(s). Paragraph A33F of ISA 500 provides relevant guidance.

⁵³ ISA 500, Paragraph A31

A128. For fair value accounting estimates, additional considerations of the relevance and reliability of information obtained from external information sources may include:

- (a) Whether fair values are based on trades of the same instrument or active market quotations;
- (b) When the fair values are based on transactions of comparable assets or liabilities, how those transactions are identified and considered comparable;
- (c) When there are no transactions either for the asset or liability or comparable assets or liabilities, how the information was developed including whether the inputs developed and used represent the assumptions that market participants would use when pricing the asset or liability, if applicable; and
- (d) When the fair value measurement is based on a broker quote, whether the broker quote:
 - (i) Is from a market maker who transacts in the same type of financial instrument;
 - (ii) Is binding or nonbinding, with more weight placed on quotes based on binding offers; and
 - (iii) Reflects market conditions as of the date of the financial statements, when required by the applicable financial reporting framework.

A129. When information from an external information source is used as audit evidence, a relevant consideration for the auditor may be whether information can be obtained, or whether the information is sufficiently detailed, to understand the methods, assumptions and other data used by the external information source. This may be limited in some respects and consequently influence the auditor's consideration of the nature, timing and extent of procedures to perform. For example, pricing services often provide information about their methods and assumptions by asset class rather than individual securities. Brokers often provide only limited information about their inputs and assumptions when providing broker indicative quotes for individual securities. Paragraph A33Ga of ISA 500 provides guidance with respect to restrictions placed by the external information source on the provision of supporting information.

Management's Expert

A130. Assumptions relating to accounting estimates that are made or identified by a management's expert become management's assumptions when used by management in making an accounting estimate. Accordingly, the auditor applies the relevant requirements in this ISA to those assumptions.

A131. If the work of a management's expert involves the use of methods or sources of data relating to accounting estimates, or developing or providing findings or conclusions relating to a point estimate or related disclosures for inclusion in the financial statements, the requirements in paragraphs 21–29 of this ISA may assist the auditor in applying paragraph 8(c) of ISA 500.

Service Organizations

A132. ISA 402⁵⁴ deals with the auditor's understanding of the services provided by a service organization, including internal control, as well as the auditor's responses to assessed risks of material misstatement. When the entity uses the services of a service organization in making accounting estimates, the requirements and guidance in ISA 402 may therefore assist the auditor in applying the requirements of this ISA.

⁵⁴ ISA 402, *Audit Considerations Relating to an Entity Using a Service Organization*

Indicators of Possible Management Bias (Ref: Para. 32)

A133. Management bias may be difficult to detect at an account level and may only be identified by the auditor when considering groups of accounting estimates, all accounting estimates in aggregate, or when observed over a number of accounting periods. For example, if accounting estimates included in the financial statements are considered to be individually reasonable but management's point estimates consistently trend toward one end of the auditor's range of reasonable outcomes that provide a more favorable financial reporting outcome for management, such circumstances may indicate possible bias by management.

A134. Examples of indicators of possible management bias with respect to accounting estimates include:

- Changes in an accounting estimate, or the method for making it, when management has made a subjective assessment that there has been a change in circumstances.
- Selection or development of significant assumptions or the data that yield a point estimate favorable for management objectives.
- Selection of a point estimate that may indicate a pattern of optimism or pessimism.

When such indicators are identified, there may be a risk of material misstatement either at the assertion or financial statement level. Indicators of possible management bias themselves do not constitute misstatements for purposes of drawing conclusions on the reasonableness of individual accounting estimates. However, in some cases the audit evidence may point to a misstatement rather than simply an indicator of management bias.

A135. Indicators of possible management bias may affect the auditor's conclusion as to whether the auditor's risk assessment and related responses remain appropriate. The auditor may also need to consider the implications for other aspects of the audit, including the need to further question the appropriateness of management's judgments in making accounting estimates. Further, indicators of possible management bias may affect the auditor's conclusion as to whether the financial statements as a whole are free from material misstatement, as discussed in ISA 700 (Revised).⁵⁵

A136. In addition, in applying ISA 240, the auditor is required to evaluate whether management's judgments and decisions in making the accounting estimates included in the financial statements indicate a possible bias that may represent a material misstatement due to fraud.⁵⁶ Fraudulent financial reporting is often accomplished through intentional misstatement of accounting estimates, which may include intentionally understating or overstating accounting estimates. Indicators of possible management bias that may also be a fraud risk factor, may cause the auditor to reassess whether the auditor's risk assessments, in particular the assessment of fraud risks, and related responses remain appropriate.

Overall Evaluation Based on Audit Procedures Performed (Ref: Para. 33)

A137. As the auditor performs planned audit procedures, the audit evidence obtained may cause the auditor to modify the nature, timing or extent of other planned audit procedures.⁵⁷ In relation to accounting estimates, information may come to the auditor's attention through performing procedures to obtain audit evidence that differs significantly from the information on which the

⁵⁵ ISA 700 (Revised), paragraph 11

⁵⁶ ISA 240, paragraph 32(b)

⁵⁷ ISA 330, paragraph A60

risk assessment was based. For example, the auditor may have identified that the only reason for an assessed risk of material misstatement is the subjectivity involved in making the accounting estimate. However, while performing procedures to respond to the assessed risks of material misstatement, the auditor may discover that the accounting estimate is more complex than originally contemplated, which may call into question the assessment of the risk of material misstatement (for example, the inherent risk may need to be re-assessed on the higher end of the spectrum of inherent risk due to the effect of complexity) and therefore the auditor may need to perform additional further audit procedures to obtain sufficient appropriate audit evidence.⁵⁸

A138. With respect to accounting estimates that have not been recognized, a particular focus of the auditor's evaluation may be on whether the recognition criteria of the applicable financial reporting framework have in fact been met. When an accounting estimate has not been recognized, and the auditor concludes that this treatment is appropriate, some financial reporting frameworks may require disclosure of the circumstances in the notes to the financial statements.

Determining Whether the Accounting Estimates are Reasonable or Misstated (Ref: Para. 9, 35)

A139. In determining whether, based on the audit procedures performed and evidence obtained, management's point estimate and related disclosures are reasonable, or are misstated:

- When the audit evidence supports a range, the size of the range may be wide and, in some circumstances, may be multiples of materiality for the financial statements as a whole (see also paragraph A125). Although a wide range may be appropriate in the circumstances, it may indicate that it is important for the auditor to reconsider whether sufficient appropriate audit evidence has been obtained regarding the reasonableness of the amounts within the range.
- The audit evidence may support a point estimate that differs from management's point estimate. In such circumstances, the difference between the auditor's point estimate and management's point estimate constitutes a misstatement.
- The audit evidence may support a range that does not include management's point estimate. In such circumstances, the misstatement is the difference between management's point estimate and the nearest point of the auditor's range.

A140. Paragraphs A110–A114 provide guidance to assist the auditor in evaluating management's selection of a point estimate and related disclosures to be included in the financial statements.

A141. When the auditor's further audit procedures include testing how management made the accounting estimate or developing an auditor's point estimate or range, the auditor is required to obtain sufficient appropriate audit evidence about disclosures that describe estimation uncertainty in accordance with paragraphs 26(b) and 29(b) and other disclosures in accordance with paragraph 31. The auditor then considers the audit evidence obtained about disclosures as part of the overall evaluation, in accordance with paragraph 35, of whether the accounting estimates and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated.

A142. ISA 450 also provides guidance regarding qualitative disclosures⁵⁹ and when misstatements in disclosures could be indicative of fraud.⁶⁰

⁵⁸ See also ISA 315 (Revised), paragraph 31

⁵⁹ ISA 450, paragraph A17

⁶⁰ ISA 450, paragraph A22

A143. When the financial statements are prepared in accordance with a fair presentation framework, the auditor's evaluation as to whether the financial statements achieve fair presentation⁶¹ includes the consideration of the overall presentation, structure and content of the financial statements, and whether the financial statements, including the related notes, represent the transactions and events in a manner that achieves fair presentation. For example, when an accounting estimate is subject to a higher degree of estimation uncertainty, the auditor may determine that additional disclosures are necessary to achieve fair presentation. If management does not include such additional disclosures, the auditor may conclude that the financial statements are materially misstated.

A144. ISA 705 (Revised)⁶² provides guidance on the implications for the auditor's opinion when the auditor believes that management's disclosures in the financial statements are inadequate or misleading, including, for example, with respect to estimation uncertainty.

Written Representations (Ref: Para. 37)

A145. Written representations about specific accounting estimates may include representations:

- That the significant judgments made in making the accounting estimates have taken into account all relevant information of which management is aware.
- About the consistency and appropriateness in the selection or application of the methods, assumptions and data used by management in making the accounting estimates.
- That the assumptions appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the entity, when relevant to the accounting estimates and disclosures.
- That disclosures related to accounting estimates, including disclosures describing estimation uncertainty, are complete and are reasonable in the context of the applicable financial reporting framework.
- That appropriate specialized skills or expertise has been applied in making the accounting estimates.
- That no subsequent event requires adjustment to the accounting estimates and related disclosures included in the financial statements.
- When accounting estimates are not recognized or disclosed in the financial statements, about the appropriateness of management's decision that the recognition or disclosure criteria of the applicable financial reporting framework have not been met.

Communication with Those Charged With Governance, Management or Other Relevant Parties (Ref: Para. 38)

A146. In applying ISA 260 (Revised), the auditor communicates with those charged with governance the auditor's views about significant qualitative aspects of the entity's accounting practices relating to accounting estimates and related disclosures.⁶³ Appendix 2 includes matters specific to accounting estimates that the auditor may consider communicating to those charged with governance.

⁶¹ ISA 700 (Revised), paragraph 14

⁶² ISA 705 (Revised), paragraphs 22–23

⁶³ ISA 260 (Revised), paragraph 16(a)

A147. ISA 265 requires the auditor to communicate in writing to those charged with governance significant deficiencies in internal control identified during the audit.⁶⁴ Such significant deficiencies may include those related to controls over:

- (a) The selection and application of significant accounting policies, and the selection and application of methods, assumptions and data;
- (b) Risk management and related systems;
- (c) Data integrity, including when data is obtained from an external information source; and
- (d) The use, development and validation of models, including models obtained from an external provider, and any adjustments that may be required.

A148. In addition to communicating with those charged with governance, the auditor may be permitted or required to communicate directly with regulators or prudential supervisors. Such communication may be useful throughout the audit or at particular stages, such as when planning the audit or when finalizing the auditor's report. For example, in some jurisdictions, financial institution regulators seek to cooperate with auditors to share information about the operation and application of controls over financial instrument activities, challenges in valuing financial instruments in inactive markets, expected credit losses, and insurance reserves while other regulators may seek to understand the auditor's views on significant aspects of the entity's operations including the entity's costs estimates. This communication may be helpful to the auditor in identifying, assessing and responding to risks of material misstatement.

Documentation (Ref: Para. 39)

A149. ISA 315 (Revised)⁶⁵ and ISA 330⁶⁶ provide requirements and guidance on documenting the auditor's understanding of the entity, risk assessments and responses to assessed risks. This guidance is based on the requirements and guidance in ISA 230.⁶⁷ In the context of auditing accounting estimates, the auditor is required to prepare audit documentation about key elements of the auditor's understanding of the entity and its environment related to accounting estimates. In addition, the auditor's judgments about the assessed risks of material misstatement related to accounting estimates, and the auditor's responses, may likely be further supported by documentation of communications with those charged with governance and management.

A150. In documenting the linkage of the auditor's further audit procedures with the assessed risks of material misstatement at the assertion level, in accordance with ISA 330, this ISA requires that the auditor take into account the reasons given to the risks of material misstatement at the assertion level. Those reasons may relate to one or more inherent risk factors or the auditor's assessment of control risk. However, the auditor is not required to document how every inherent risk factor was taken into account in identifying and assessing the risks of material misstatement in relation to each accounting estimate.

A151. The auditor also may consider documenting:

- When management's application of the method involves complex modeling, whether management's judgments have been applied consistently and, when applicable, that the

⁶⁴ ISA 265, paragraph 9

⁶⁵ ISA 315 (Revised), paragraphs 32 and A152–A155

⁶⁶ ISA 330, paragraphs 28 and A63

⁶⁷ ISA 230, paragraph 8(c)

design of the model meets the measurement objective of the applicable financial reporting framework.

- When the selection and application of methods, significant assumptions, or the data is affected by complexity to a higher degree, the auditor's judgments in determining whether specialized skills or knowledge are required to perform the risk assessment procedures, to design and perform procedures responsive to those risks, or to evaluate the audit evidence obtained. In these circumstances, the documentation also may include how the required skills or knowledge were applied.

A152. Paragraph A7 of ISA 230 notes that, although there may be no single way in which the auditor's exercise of professional skepticism is documented, the audit documentation may nevertheless provide evidence of the auditor's exercise of professional skepticism. For example, in relation to accounting estimates, when the audit evidence obtained includes evidence that both corroborates and contradicts management's assertions, the documentation may include how the auditor evaluated that evidence, including the professional judgments made in forming a conclusion as to the sufficiency and appropriateness of the audit evidence obtained. Examples of other requirements in this ISA for which documentation may provide evidence of the exercise of professional skepticism by the auditor include:

- Paragraph 13(d), regarding how the auditor has applied an understanding in developing the auditor's own expectation of the accounting estimates and related disclosures to be included in the entity's financial statements and how that expectation compares with the entity's financial statements prepared by management;
- Paragraph 18, which requires further audit procedures to be designed and performed to obtain sufficient appropriate evidence in a manner that is not biased toward obtaining audit evidence that may be corroborative or towards excluding audit evidence that may be contradictory;
- Paragraphs 23(b), 24(b), 25(b) and 32, which address indicators of possible management bias; and
- Paragraph 34, which addresses the auditor's consideration of all relevant audit evidence, whether corroborative or contradictory.

Appendix 1

(Ref: Para. 2, 4, 12(c), A8, A66)

Inherent Risk Factors

Introduction

1. In identifying, assessing and responding to the risks of material misstatement at the assertion level for an accounting estimate and related disclosures, this ISA requires the auditor to take into account the degree to which the accounting estimate is subject to estimation uncertainty, and the degree to which the selection and application of the methods, assumptions and data used in making the accounting estimate, and the selection of management's point estimate and related disclosures for inclusion in the financial statements, are affected by complexity, subjectivity or other inherent risk factors.
2. Inherent risk related to an accounting estimate is the susceptibility of an assertion about the accounting estimate to material misstatement, before consideration of controls. Inherent risk results from inherent risk factors, which give rise to challenges in appropriately making the accounting estimate. This Appendix provides further explanation about the nature of the inherent risk factors of estimation uncertainty, subjectivity and complexity, and their inter-relationships, in the context of making accounting estimates and selecting management's point estimate and related disclosures for inclusion in the financial statements.

Measurement Basis

3. The measurement basis and the nature, condition and circumstances of the financial statement item give rise to relevant valuation attributes. When the cost or price of the item cannot be directly observed, an accounting estimate is required to be made by applying an appropriate method and using appropriate data and assumptions. The method may be specified by the applicable financial reporting framework, or is selected by management, to reflect the available knowledge about how the relevant valuation attributes would be expected to influence the cost or price of the item on the measurement basis.

Estimation Uncertainty

4. Susceptibility to a lack of precision in measurement is often referred to in accounting frameworks as measurement uncertainty. Estimation uncertainty is defined in this ISA as susceptibility to an inherent lack of precision in measurement. It arises when the required monetary amount for a financial statement item that is recognized or disclosed in the financial statements cannot be measured with precision through direct observation of the cost or price. When direct observation is not possible, the next most precise alternative measurement strategy is to apply a method that reflects the available knowledge about cost or price for the item on the relevant measurement basis, using observable data about relevant valuation attributes.
5. However, constraints on the availability of such knowledge or data may limit the verifiability of such inputs to the measurement process and therefore limit the precision of measurement outcomes. Furthermore, most accounting frameworks acknowledge that there are practical constraints on the information that should be taken into account, such as when the cost of obtaining it would exceed the benefits. The lack of precision in measurement arising from these constraints is inherent because it cannot be eliminated from the measurement process. Accordingly, such constraints are sources of estimation uncertainty. Other sources of measurement uncertainty that may occur in the measurement process are, at least in principle,

capable of elimination if the method is applied appropriately and therefore are sources of potential misstatement rather than estimation uncertainty.

6. When estimation uncertainty relates to uncertain future inflows or outflows of economic benefits that will ultimately result from the underlying asset or liability, the outcome of these flows will only be observable after the date of the financial statements. Depending on the nature of the applicable measurement basis and on the nature, condition and circumstances of the financial statement item, this outcome may be directly observable before the financial statements are finalized or may only be directly observable at a later date. For some accounting estimates, there may be no directly observable outcome at all.
7. Some uncertain outcomes may be relatively easy to predict with a high level of precision for an individual item. For example, the useful life of a production machine may be easily predicted if sufficient technical information is available about its average useful life. When it is not possible to predict a future outcome, such as an individual's life expectancy based on actuarial assumptions, with reasonable precision, it may still be possible to predict that outcome for a group of individuals with greater precision. Measurement bases may, in some cases, indicate a portfolio level as the relevant unit of account for measurement purposes, which may reduce inherent estimation uncertainty.

Complexity

8. Complexity (i.e., the complexity inherent in the process of making an accounting estimate, before consideration of controls) gives rise to inherent risk. Inherent complexity may arise when:
 - There are many valuation attributes with many or non-linear relationships between them.
 - Determining appropriate values for one or more valuation attributes requires multiple data sets.
 - More assumptions are required in making the accounting estimate, or when there are correlations between the required assumptions.
 - The data used is inherently difficult to identify, capture, access or understand.
9. Complexity may be related to the complexity of the method and of the computational process or model used to apply it. For example, complexity in the model may reflect the need to apply probability-based valuation concepts or techniques, option pricing formulae or simulation techniques to predict uncertain future outcomes or hypothetical behaviors. Similarly, the computational process may require data from multiple sources, or multiple data sets to support the making of an assumption or the application of sophisticated mathematical or statistical concepts.
10. The greater the complexity, the more likely it is that management will need to apply specialized skills or knowledge in making an accounting estimate or engage a management's expert, for example in relation to:
 - Valuation concepts and techniques that could be used in the context of the measurement basis and objectives or other requirements of the applicable financial reporting framework and how to apply those concepts or techniques;
 - The underlying valuation attributes that may be relevant given the nature of the measurement basis and the nature, condition and circumstances of the financial statement items for which accounting estimates are being made; or

- Identifying appropriate sources of data from internal sources (including from sources outside the general or subsidiary ledgers) or from external information sources, determining how to address potential difficulties in obtaining data from such sources or in maintaining its integrity in applying the method, or understanding the relevance and reliability of that data.
11. Complexity relating to data may arise, for example, in the following circumstances:
- (a) When data is difficult to obtain or when it relates to transactions that are not generally accessible. Even when such data is accessible, for example through an external information source, it may be difficult to consider the relevance and reliability of the data, unless the external information source discloses adequate information about the underlying data sources it has used and about any data processing that has been performed.
 - (b) When data reflecting an external information source's views about future conditions or events, which may be relevant in developing support for an assumption, is difficult to understand without transparency about the rationale and information taken into account in developing those views.
 - (c) When certain types of data are inherently difficult to understand because they require an understanding of technically complex business or legal concepts, such as may be required to properly understand data that comprises the terms of legal agreements about transactions involving complex financial instruments or insurance products.

Subjectivity

12. Subjectivity (i.e., the subjectivity inherent in the process of making an accounting estimate, before consideration of controls) reflects inherent limitations in the knowledge or data reasonably available about valuation attributes. When such limitations exist, the applicable financial reporting framework may reduce the degree of subjectivity by providing a required basis for making certain judgments. Such requirements may, for example, set explicit or implied objectives relating to measurement, disclosure, the unit of account, or the application of a cost constraint. The applicable financial reporting framework may also highlight the importance of such judgments through requirements for disclosures about those judgments.
13. Management judgment is generally needed in determining some or all of the following matters, which often involve subjectivity:
- To the extent not specified under the requirements of the applicable financial reporting framework, the appropriate valuation approaches, concepts, techniques and factors to use in the estimation method, having regard to available knowledge;
 - To the extent valuation attributes are observable when there are various potential sources of data, the appropriate sources of data to use;
 - To the extent valuation attributes are not observable, the appropriate assumptions or range of assumptions to make, having regard to the best available data, including, for example, market views;
 - The range of reasonably possible outcomes from which to select management's point estimate, and the relative likelihood that certain points within that range would be consistent with the objectives of the measurement basis required by the applicable financial reporting framework; and
 - The selection of management's point estimate, and the related disclosures to be made, in the financial statements.

14. Making assumptions about future events or conditions involves the use of judgment, the difficulty of which varies with the degree to which those events or conditions are uncertain. The precision with which it is possible to predict uncertain future events or conditions depends on the degree to which those events or conditions are determinable based on knowledge, including knowledge of past conditions, events and related outcomes. The lack of precision also contributes to estimation uncertainty, as described above.
15. With respect to future outcomes, assumptions will only need to be made for those features of the outcome that are uncertain. For example, in considering the measurement of a possible impairment of a receivable for a sale of goods at the balance sheet date, the amount of the receivable may be unequivocally established and directly observable in the related transaction documents. What may be uncertain is the amount, if any, for loss due to impairment. In this case, assumptions may only be required about the likelihood of loss and about the amount and timing of any such loss.
16. However, in other cases, the amounts of cash flows embodied in the rights relating to an asset may be uncertain. In those cases, assumptions may have to be made about both the amounts of the underlying rights to cash flows and about potential losses due to impairment.
17. It may be necessary for management to consider information about past conditions and events, together with current trends and expectations about future developments. Past conditions and events provide historical information that may highlight repeating historical patterns that can be extrapolated in evaluating future outcomes. Such historical information may also indicate changing patterns of such behavior over time (cycles or trends). These may suggest that the underlying historical patterns of behavior have been changing in somewhat predictable ways that may also be extrapolated in evaluating future outcomes. Other types of information may also be available that indicate possible changes in historical patterns of such behavior or in related cycles or trends. Difficult judgments may be needed about the predictive value of such information.
18. The extent and nature (including the degree of subjectivity involved) of the judgments taken in making the accounting estimates may create opportunity for management bias in making decisions about the course of action that, according to management, is appropriate in making the accounting estimate. When there is also a high level of complexity or a high level of estimation uncertainty, or both, the risk of, and opportunity for, management bias or fraud may also be increased.

Relationship of Estimation Uncertainty to Subjectivity and Complexity

19. Estimation uncertainty gives rise to inherent variation in the possible methods, data sources and assumptions that could be used to make an accounting estimate. This gives rise to subjectivity, and hence, the need for the use of judgment in making the accounting estimate. Such judgments are required in selecting the appropriate methods and data sources, in making the assumptions, and in selecting management's point estimate and related disclosures for inclusion in the financial statements. These judgments are made in the context of the recognition, measurement, presentation and disclosure requirements of the applicable financial reporting framework. However, because there are constraints on the availability and accessibility of knowledge or information to support these judgments, they are subjective in nature.
20. Subjectivity in such judgments creates the opportunity for unintentional or intentional management bias in making them. Many accounting frameworks require that information prepared for inclusion in the financial statements should be neutral (i.e., that it should not be biased). Given that bias can, at least in principle, be eliminated from the estimation process,

sources of potential bias in the judgments made to address subjectivity are sources of potential misstatement rather than sources of estimation uncertainty.

21. The inherent variation in the possible methods, data sources and assumptions that could be used to make an accounting estimate (see paragraph 19) also gives rise to variation in the possible measurement outcomes. The size of the range of reasonably possible measurement outcomes results from the degree of estimation uncertainty and is often referred to as the sensitivity of the accounting estimate. In addition to determining measurement outcomes, an estimation process also involves analyzing the effect of inherent variations in the possible methods, data sources and assumptions on the range of reasonably possible measurement outcomes (referred to as sensitivity analysis).
22. Developing a financial statement presentation for an accounting estimate, which, when required by the applicable financial reporting framework, achieves faithful representation (i.e., complete, neutral and free from error) includes making appropriate judgments in selecting a management point estimate that is appropriately chosen from within the range of reasonably possible measurement outcomes and related disclosures that appropriately describe the estimation uncertainty. These judgments may themselves involve subjectivity, depending on the nature of the requirements in the applicable financial reporting framework that address these matters. For example, the applicable financial reporting framework may require a specific basis (such as a probability weighted average or a best estimate) for the selection of the management point estimate. Similarly, it may require specific disclosures or disclosures that meet specified disclosure objectives or additional disclosures that are required to achieve fair presentation in the circumstances.
23. Although an accounting estimate that is subject to a higher degree of estimation uncertainty may be less precisely measurable than one subject to a lower degree of estimation uncertainty, the accounting estimate may still have sufficient relevance for users of the financial statements to be recognized in the financial statements if, when required by the applicable financial reporting framework, a faithful representation of the item can be achieved. In some cases, estimation uncertainty may be so great that the recognition criteria in the applicable financial reporting framework are not met and the accounting estimate cannot be recognized in the financial statements. Even in these circumstances, there may still be relevant disclosure requirements, for example to disclose the point estimate or range of reasonably possible measurement outcomes and information describing the estimation uncertainty and constraints in recognizing the item. The requirements of the applicable financial reporting framework that apply in these circumstances may be specified to a greater or lesser degree. Accordingly, in these circumstances, there may be additional judgments that involve subjectivity to be made.

Appendix 2

(Ref: Para. A146)

Communications with Those Charged with Governance

Matters that the auditor may consider communicating with those charged with governance with respect to the auditor's views about significant qualitative aspects of the entity's accounting practices related to accounting estimates and related disclosures include:

- (a) How management identifies transactions, other events and conditions that may give rise to the need for, or changes in, accounting estimates and related disclosures.
- (b) Risks of material misstatement.
- (c) The relative materiality of the accounting estimates to the financial statements as a whole;
- (d) Management's understanding (or lack thereof) regarding the nature and extent of, and the risks associated with, accounting estimates;
- (e) Whether management has applied appropriate specialized skills or knowledge or engaged appropriate experts.
- (f) The auditor's views about differences between the auditor's point estimate or range and management's point estimate.
- (g) The auditor's views about the appropriateness of the selection of accounting policies related to accounting estimates and presentation of accounting estimates in the financial statements.
- (h) Indicators of possible management bias.
- (i) Whether there has been or ought to have been a change from the prior period in the methods for making the accounting estimates
- (j) When there has been a change from the prior period in the methods for making the accounting estimate, why, as well as the outcome of accounting estimates in prior periods.
- (k) Whether management's methods for making the accounting estimates, including when management has used a model, are appropriate in the context of the measurement objectives, the nature, conditions and circumstances, and other requirements of the applicable financial reporting framework.
- (l) The nature and consequences of significant assumptions used in accounting estimates and the degree of subjectivity involved in the development of the assumptions;
- (m) Whether significant assumptions are consistent with each other and with those used in other accounting estimates, or with assumptions used in other areas of the entity's business activities.
- (n) When relevant to the appropriateness of the significant assumptions or the appropriate application of the applicable financial reporting framework, whether management has the intent to carry out specific courses of action and has the ability to do so.
- (o) How management has considered alternative assumptions or outcomes and why it has rejected them, or how management has otherwise addressed estimation uncertainty in making the accounting estimate.
- (p) Whether the data and significant assumptions used by management in making the accounting estimates are appropriate in the context of the applicable financial reporting framework.

- (q) The relevance and reliability of information obtained from an external information source.
- (r) Significant difficulties encountered when obtaining sufficient appropriate audit evidence relating to data obtained from an external information source or valuations performed by management or a management's expert.
- (s) Significant differences in judgments between the auditor and management or a management's expert regarding valuations.
- (t) The potential effects on the entity's financial statements of material risks and exposures required to be disclosed in the financial statements, including the estimation uncertainty associated with accounting estimates.
- (u) The reasonableness of disclosures about estimation uncertainty in the financial statements.
- (v) Whether management's decisions relating to the recognition, measurement, presentation and disclosure of the accounting estimates and related disclosures in the financial statements are in accordance with the applicable financial reporting framework.

CONFORMING AND CONSEQUENTIAL AMENDMENTS TO OTHER INTERNATIONAL STANDARDS ARISING FROM ISA 540 (Revised)¹

Note: The following are conforming amendments to other International Standards as a result of the approval of ISA 540 (Revised). These amendments will become effective at the same time as ISA 540 (Revised), and are shown with marked changes from the latest approved versions of the International Standards that are amended. The footnote numbers within these amendments do not align with the International Standards that are amended, and reference should be made to those International Standards.

ISA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With International Standards on Auditing

Application and Other Explanatory Material

...

Sufficient Appropriate Audit Evidence and Audit Risk (Ref: Para. 5 and 17)

...

Audit Risk

...

Risks of Material Misstatement

...

A42. The assessment of the risks of material misstatement may be expressed in quantitative terms, such as in percentages, or in non-quantitative terms. In any case, the need for the auditor to make appropriate risk assessments is more important than the different approaches by which they may be made. The ISAs do not ordinarily refer to inherent risk and control risk separately, but rather to a combined assessment of the “risks of material misstatement.” However, ISA 540 (Revised)² requires a separate assessment of inherent risk and control risk to provide a basis for designing and performing further audit procedures to respond to the assessed risks of material misstatement, including significant risks, for accounting estimates at the assertion level in accordance with ISA 330.³ In identifying and assessing risks of material misstatement for significant classes of transactions, account balances or disclosures other than accounting estimates, the auditor may make separate or combined assessments of inherent and control risk depending on preferred audit techniques or methodologies and practical considerations. ~~The assessment of the risks of material misstatement may be expressed in quantitative terms, such as in percentages, or in non-quantitative terms. In any case, the need for the auditor to make appropriate risk assessments is more important than the different approaches by which they may be made.~~

¹ Draft Proposed ISA 540 (Revised), *Auditing Accounting Estimates and Disclosures*

² ISA 540 (Revised), *Auditing Accounting Estimates and Disclosures*, paragraph 15

³ ISA 330, paragraph 7(b)

ISA 230, *Audit Documentation*

Requirements

...

Documentation of the Audit Procedures Performed and Audit Evidence Obtained

Form, Content and Extent of Audit Documentation

8. The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand: (Ref: Para. A2–A5, A16–A17)
- (a) The nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements; (Ref: Para. A6–A7)
 - (b) The results of the audit procedures performed, and the audit evidence obtained; and
 - (c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. (Ref: Para. A8–A11)

...

Application and Other Explanatory Material

...

Documentation of Compliance with ISAs (Ref: Para. 8(a))

...

- A7. Audit documentation provides evidence that the audit complies with the ISAs. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file. For example:
- The existence of an adequately documented audit plan demonstrates that the auditor has planned the audit.
 - The existence of a signed engagement letter in the audit file demonstrates that the auditor has agreed the terms of the audit engagement with management or, where appropriate, those charged with governance.
 - An auditor's report containing an appropriately qualified opinion on the financial statements demonstrates that the auditor has complied with the requirement to express a qualified opinion under the circumstances specified in the ISAs.
 - In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:
 - For example, there may be no single way in which the auditor's professional skepticism is documented. But the audit documentation may nevertheless provide evidence of the auditor's exercise of professional skepticism in accordance with the ISAs. For example, in relation to accounting estimates, when the audit evidence obtained includes evidence

that both corroborates and contradicts management's assertions, documenting how the auditor evaluated that evidence, including the professional judgments made in forming a conclusion as to the sufficiency and appropriateness of the audit evidence obtained. Such evidence may include specific procedures performed to corroborate management's responses to the auditor's inquiries.

- Similarly, that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the ISAs may be evidenced in a number of ways within the audit documentation. This may include documentation of the engagement partner's timely involvement in aspects of the audit, such as participation in the team discussions required by ISA 315 (Revised).⁴

...

Documentation of Significant Matters and Related Significant Professional Judgments (Ref: Para. 8(c))

...

A10. Some examples of circumstances in which, in accordance with paragraph 8, it is appropriate to prepare audit documentation relating to the use of professional judgment include, where the matters and judgments are significant:

- The rationale for the auditor's conclusion when a requirement provides that the auditor "shall consider" certain information or factors, and that consideration is significant in the context of the particular engagement.
- The basis for the auditor's conclusion on the reasonableness of areas of subjective judgments made by management ~~(for example, the reasonableness of significant accounting estimates).~~
- The basis for the auditor's evaluation of whether an accounting estimate and related disclosures are reasonable in the context of the applicable financial reporting framework, or are misstated.
- The basis for the auditor's conclusions about the authenticity of a document when further investigation (such as making appropriate use of an expert or of confirmation procedures) is undertaken in response to conditions identified during the audit that caused the auditor to believe that the document may not be authentic.
- When ISA 701 applies,⁵ the auditor's determination of the key audit matters or the determination that there are no key audit matters to be communicated.

⁴ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 10

⁵ ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

Appendix

(Ref: Para 1)

Specific Audit Documentation Requirements in Other ISAs

...

- ISA 540 (Revised), Auditing Accounting Estimates, ~~Including Fair Value Accounting Estimates~~, and Related Disclosures – paragraph 37~~23~~

...

ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements Accounting Estimates*

Application and Other Explanatory Material

...

A47. A retrospective review is also required by ISA 540 (Revised). That review is conducted as a risk assessment procedure to obtain information regarding the effectiveness of management's previous ~~prior period estimation process~~ accounting estimates, audit evidence about the outcome, or where applicable, their subsequent re-estimation of ~~prior period accounting estimates that is pertinent to making~~ to assist in identifying and assessing the risks of material misstatement in the current period ~~accounting estimates~~, and audit evidence of matters, such as estimation uncertainty, that may be required to be disclosed in the financial statements. As a practical matter, the auditor's review of management judgments and assumptions for biases that could represent a risk of material misstatement due to fraud in accordance with this ISA may be carried out in conjunction with the review required by ISA 540 (Revised).

...

ISA 260 (Revised), *Communication with Those Charged with Governance*

Requirements

...

Matters to Be Communicated

...

Significant Findings from the Audit

16. The auditor shall communicate with those charged with governance: (Ref: Para. A17–A18)
- a) The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures. When applicable, the auditor shall explain to those charged with governance why the auditor considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate to the particular circumstances of the entity; (Ref: Para. A19–A20)
 - b) Significant difficulties, if any, encountered during the audit; (Ref: Para. A21)
 - c) Unless all of those charged with governance are involved in managing the entity:
 - (i) Significant matters arising during the audit that were discussed, or subject to correspondence, with management; and (Ref: Para. A22)
 - (ii) Written representations the auditor is requesting;
 - d) Circumstances that affect the form and content of the auditor's report, if any; and (Ref: Para. A23–A25)
 - e) Any other significant matters arising during the audit that, in the auditor's professional judgment, are relevant to the oversight of the financial reporting process. (Ref: Para. A26–A28)

...

Application and Other Explanatory Material

...

Matters to Be Communicated

...

Significant Findings from the Audit

...

Significant Qualitative Aspects of Accounting Practices (Ref: Para. 16(a))

- A19. Financial reporting frameworks ordinarily allow for the entity to make accounting estimates, and judgments about accounting policies and financial statement disclosures, for example, in relation to the use of key assumptions in the development of accounting estimates for which there is significant

~~measurement uncertainty.~~ In addition, law, regulation or financial reporting frameworks may require disclosure of a summary of significant accounting policies or make reference to “critical accounting estimates” or “critical accounting policies and practices” to identify and provide additional information to users about the most difficult, subjective or complex judgments made by management in preparing the financial statements.

- A20. As a result, the auditor's views on the subjective aspects of the financial statements may be particularly relevant to those charged with governance in discharging their responsibilities for oversight of the financial reporting process. For example, in relation to the matters described in paragraph A19, those charged with governance may be interested in the auditor's ~~evaluation of the adequacy of disclosures of the estimation uncertainty relating to accounting estimates that give rise to significant risks.~~ views on the degree to which complexity, subjectivity or other inherent risk factors affect the selection or application of the methods, assumptions and data used in making a significant accounting estimate, as well as the auditor's evaluation of whether management's point estimate and related disclosures in the financial statements are reasonable in the context of the applicable financial reporting framework. Open and constructive communication about significant qualitative aspects of the entity's accounting practices also may include comment on the acceptability of significant accounting practices and on the quality of the disclosures. When applicable, this may include whether a significant accounting practice of the entity relating to accounting estimates is considered by the auditor not to be most appropriate to the particular circumstances of the entity, for example, when an alternative acceptable method for making an accounting estimate would, in the auditor's judgment, be more appropriate. Appendix 2 identifies matters that may be included in this communication.

...

Appendix 1

(Ref: Para. 3)

Specific Requirements in ISQC 1 and Other ISAs that Refer to Communications with Those Charged With Governance

This appendix identifies paragraphs in ISQC 1⁶ and other ISAs that require communication of specific matters with those charged with governance. The list is not a substitute for considering the requirements and related application and other explanatory material in ISAs.

- ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* – paragraph 30(a)
- ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements* – paragraphs 21, 38(c)(i) and 40-42
- ISA 250, *Consideration of Laws and Regulations in an Audit of Financial Statements* – paragraphs 14, 19 and 22-24
- ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* – paragraph 9
- ISA 450, *Evaluation of Misstatements Identified during the Audit* – paragraphs 12-13
- ISA 505, *External Confirmations* – paragraph 9
- ISA 510, *Initial Audit Engagements—Opening Balances* – paragraph 7
- ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures* – paragraph 36
- ISA 550, *Related Parties* – paragraph 27
- ISA 560, *Subsequent Events* – paragraphs 7(b)-(c), 10(a), 13(b), 14(a) and 17
- ISA 570 (Revised), *Going Concern* – paragraph 25
- ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)* – paragraph 49
- ISA 610 (Revised 2013), *Using the Work of Internal Auditors* – paragraphs 20 and 31
- ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements* – paragraph 46
- ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report* – paragraph 17
- ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report* – paragraphs 12, 14, 23 and 30
- ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* – paragraph 12
- ISA 710, *Comparative Information—Corresponding Figures and Comparative Financial Statements* – paragraph 18
- ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information* – paragraph 17—19

⁶ ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

Appendix 2

(Ref: Para. 16(a), A19–A20)

Qualitative Aspects of Accounting Practices

The communication required by paragraph 16(a), and discussed in paragraphs A19–A20, may include such matters as:

Accounting Policies

...

Accounting Estimates and Related Disclosures

~~For items for which estimates are significant, issues discussed in ISA 540,⁷ including, for example: Appendix 2 of ISA 540 (Revised) includes matters that the auditor may consider communicating with respect to significant qualitative aspects of the entity's accounting practices related to accounting estimates and related disclosures.~~

- ~~☞ How management identifies those transactions, events and conditions that may give rise to the need for accounting estimates to be recognized or disclosed in the financial statements.~~
- ~~☞ Changes in circumstances that may give rise to new, or the need to revise existing, accounting estimates.~~
- ~~☞ Whether management's decision to recognize, or to not recognize, the accounting estimates in the financial statements is in accordance with the applicable financial reporting framework.~~
- ~~☞ Whether there has been or ought to have been a change from the prior period in the methods for making the accounting estimates and, if so, why, as well as the outcome of accounting estimates in prior periods.~~
- ~~☞ Management's process for making accounting estimates (e.g., when management has used a model), including whether the selected measurement basis for the accounting estimate is in accordance with the applicable financial reporting framework.~~
- ~~☞ Whether the significant assumptions used by management in developing the accounting estimate are reasonable.~~
- ~~☞ Where relevant to the reasonableness of the significant assumptions used by management or the appropriate application of the applicable financial reporting framework, management's intent to carry out specific courses of action and its ability to do so.~~
- ~~☞ Risks of material misstatement.~~
- ~~☞ Indicators of possible management bias.~~
- ~~☞ How management has considered alternative assumptions or outcomes and why it has rejected them, or how management has otherwise addressed estimation uncertainty in making the accounting estimate.~~

⁷—ISA 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*

- ⇒ ~~The adequacy of disclosure of estimation uncertainty in the financial statements.~~

Financial Statement Disclosures

...

ISA 500, *Audit Evidence*

Introduction

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) explains what constitutes audit evidence in an audit of financial statements, and deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.
2. This ISA is applicable to all the audit evidence obtained during the course of the audit. Other ISAs deal with specific aspects of the audit (for example, ISA 315 (Revised)⁸), the audit evidence to be obtained in relation to a particular topic (for example, ISA 570 (Revised)⁹), specific procedures to obtain audit evidence (for example, ISA 520¹⁰), and the evaluation of whether sufficient appropriate audit evidence has been obtained (ISA 200¹¹ and ISA 330¹²).

Effective Date

3. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2009.

Objective

4. The objective of the auditor is to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.

Definitions

5. For purposes of ~~the~~this ISA, the following terms have the meanings attributed below:
 - (a) Accounting records – The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures.
 - (b) Appropriateness (of audit evidence) – The measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based.

⁸ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

⁹ ISA 570 (Revised), *Going Concern*

¹⁰ ISA 520, *Analytical Procedures*

¹¹ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

¹² ISA 330, *The Auditor's Responses to Assessed Risks*

- (c) Audit evidence – Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and information obtained from other sources.
- (cA) External information source – An external individual or organization that provides information that has been used by the entity in preparing the financial statements, or that has been obtained by the auditor as audit evidence, when such information is suitable for use by a broad range of users. When information has been provided by an individual or organization acting in the capacity of a management's expert, service organization¹³, or auditor's expert¹⁴ the individual or organization is not considered an external information source with respect to that particular information. (Ref: Para. A1A-A1C)
- (d) Management's expert – An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.
- (e) Sufficiency (of audit evidence) – The measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor's assessment of the risks of material misstatement and also by the quality of such audit evidence.

Requirements

Sufficient Appropriate Audit Evidence

- 6. The auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence. (Ref: Para. A1-A25)

Information to Be Used as Audit Evidence

- 7. When designing and performing audit procedures, the auditor shall consider the relevance and reliability of the information to be used as audit evidence, including information obtained from an external information source. (Ref: Para. A26–~~A33~~–A33H)
- 8. If information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes: (Ref: Para. A34–A36)
 - (a) Evaluate the competence, capabilities and objectivity of that expert; (Ref: Para. A37–A43)
 - (b) Obtain an understanding of the work of that expert; and (Ref: Para. A44–A47)
 - (c) Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion. (Ref: Para. A48)
- 9. When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes, including, as necessary in the circumstances:
 - (a) Obtaining audit evidence about the accuracy and completeness of the information; and (Ref: Para. A49–A50)

¹³ ISA 402, *Audit Considerations Relating to an Entity Using a Service Organization*, paragraph 8.

¹⁴ ISA 620, *Using the Work of an Auditor's Expert*, paragraph 6

- (b) Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes. (Ref: Para. A51)

Selecting Items for Testing to Obtain Audit Evidence

10. When designing tests of controls and tests of details, the auditor shall determine means of selecting items for testing that are effective in meeting the purpose of the audit procedure. (Ref: Para. A52-A56)

Inconsistency in, or Doubts over Reliability of, Audit Evidence

11. If:
- (a) audit evidence obtained from one source is inconsistent with that obtained from another; or
 - (b) the auditor has doubts over the reliability of information to be used as audit evidence,
- the auditor shall determine what modifications or additions to audit procedures are necessary to resolve the matter, and shall consider the effect of the matter, if any, on other aspects of the audit. (Ref: Para. A57)

Application and Other Explanatory Material

External Information Source (Ref: Para 5(cA))

A1B. External information sources may include pricing services, governmental organizations, central banks or recognized stock exchanges. Examples of information that may be obtained from external information sources include:

- Prices and pricing related data;
- Macro-economic data, such as historical and forecast unemployment rates and economic growth rates, or census data;
- Credit history data;
- Industry specific data, such as an index of reclamation costs for certain extractive industries, or viewership information or ratings used to determine advertising revenue in the entertainment industry; and
- Mortality tables used to determine liabilities in the life insurance and pension sectors.

A1Aa. A particular set of information is more likely to be suitable for use by a broad range of users and less likely to be subject to influence by any particular user if the external individual or organization provides it to the public for free, or makes it available to a wide range of users in return for payment of a fee. Judgment may be required in determining whether the information is suitable for use by a broad range of users, taking into account the ability of the entity to influence the external information source.

A1C. An external individual or organization cannot, in respect of any particular set of information, be both an external information source and a management's expert, or service organization or auditor's expert.

A1Ca. However, an external individual or organization may, for example, be acting as a management's expert when providing a particular set of information, but may be acting as an external information

source when providing a different set of information. In some circumstances, professional judgment may be needed to determine whether an external individual or organization is acting as an external information source or as a management's expert with respect to a particular set of information. In other circumstances, the distinction may be clear. For example:

- An external individual or organization may be providing information about real estate prices that is suitable for use by a broad range of users, for example, information made generally available pertaining to a geographical region, and be determined to be an external information source with respect to that set of information. The same external organization may also be acting as a management's or auditor's expert in providing commissioned valuations, with respect to the entity's real estate portfolio specifically tailored for the entity's facts and circumstances.
- Some actuarial organizations publish mortality tables for general use which, when used by an entity, would generally be considered to be information from an external information source. The same actuarial organization may also be a management's expert with respect to different information tailored to the specific circumstances of the entity to help management determine the pension liability for several of the entity's pension plans.
- An external individual or organization may possess expertise in the application of models to estimate the fair value of securities for which there is no observable market. If the external individual or organization applies that expertise in making an estimate specifically for the entity and that work is used by management in preparing its financial statements, the external individual or organization is likely to be a management's expert with respect to that information. If, on the other hand, that external individual or organization merely provides, to the public, prices or pricing-related data regarding private transactions, and the entity uses that information in its own estimation methods, the external individual or organization is likely to be an external information source with respect to such information.
- An external individual or organization may publish information, suitable for a broad range of users, about risks or conditions in an industry. If used by an entity in preparing its risk disclosures (for example in compliance with IFRS 7¹⁵), such information would ordinarily be considered to be information from an external information source. However, if the same type of information has been specifically commissioned by the entity to use its expertise to develop information about those risks, tailored to the entity's circumstances, the external individual or organization is likely to be acting as a management's expert.
- An external individual or organization may apply its expertise in providing information about current and future market trends, which it makes available to, and is suitable for use by, a broad range of users. If used by the entity to help make decisions about assumptions to be used in making accounting estimates, such information is likely to be considered to be information from an external information source. If the same type of information has been commissioned by the entity to address current and future trends relevant to the entity's specific facts and circumstances, the external individual or organization is likely to be acting as a management's expert.

¹⁵ International Financial Reporting Standards 7 (IFRS), Financial Instruments: Disclosures

Sufficient Appropriate Audit Evidence (Ref: Para. 6)

- A1. Audit evidence is necessary to support the auditor's opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit¹⁶) or a firm's quality control procedures for client acceptance and continuance. In ~~addition to other sources inside and outside the entity,~~ the entity's accounting records and other sources internal to the entity are an important source of audit evidence. ~~Also, information~~Information that may be used as audit evidence may have been prepared using the work of a management's expert, or be obtained from an external information source. Audit evidence comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions. In addition, in some cases the absence of information (for example, management's refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence
- A2. Most of the auditor's work in forming the auditor's opinion consists of obtaining and evaluating audit evidence. Audit procedures to obtain audit evidence can include inspection, observation, confirmation, recalculation, reperformance, and analytical procedures, often in some combination, in addition to inquiry. Although inquiry may provide important audit evidence, and may even produce evidence of a misstatement, inquiry alone ordinarily does not provide sufficient audit evidence of the absence of a material misstatement at the assertion level, nor of the operating effectiveness of controls.
- A3. As explained in ISA 200,¹⁷ reasonable assurance is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level.
- A4. The sufficiency and appropriateness of audit evidence are interrelated. Sufficiency is the measure of the quantity of audit evidence. The quantity of audit evidence needed is affected by the auditor's assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality.
- A5. Appropriateness is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor's opinion is based. The reliability of evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained.
- A6. ISA 330 requires the auditor to conclude whether sufficient appropriate audit evidence has been obtained.¹⁸ Whether sufficient appropriate audit evidence has been obtained to reduce audit risk to an acceptably low level, and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion, is a matter of professional judgment. ISA 200 contains discussion of such matters as the nature of audit procedures, the timeliness of financial reporting, and the balance

¹⁶ ISA 315 (Revised), paragraph 9

¹⁷ ISA 200, paragraph 5

¹⁸ ISA 330, paragraph 26

between benefit and cost, which are relevant factors when the auditor exercises professional judgment regarding whether sufficient appropriate audit evidence has been obtained.

Sources of Audit Evidence

- A7. Some audit evidence is obtained by performing audit procedures to test the accounting records, for example, through analysis and review, reperforming procedures followed in the financial reporting process, and reconciling related types and applications of the same information. Through the performance of such audit procedures, the auditor may determine that the accounting records are internally consistent and agree to the financial statements.
- A8. More assurance is ordinarily obtained from consistent audit evidence obtained from different sources or of a different nature than from items of audit evidence considered individually. For example, corroborating information obtained from a source independent of the entity may increase the assurance the auditor obtains from audit evidence that is generated internally, such as evidence existing within the accounting records, minutes of meetings, or a management representation.
- A9. Information from sources independent of the entity that the auditor may use as audit evidence may include confirmations from third parties, and information from an external information source, including analysts' reports, and comparable data about competitors (benchmarking data).

Audit Procedures for Obtaining Audit Evidence

- A10. As required by, and explained further in, ISA 315 (Revised) and ISA 330, audit evidence to draw reasonable conclusions on which to base the auditor's opinion is obtained by performing:
- (a) Risk assessment procedures; and
 - (b) Further audit procedures, which comprise:
 - (i) Tests of controls, when required by the ISA or when the auditor has chosen to do so; and
 - (ii) Substantive procedures, including tests of details and substantive analytical procedures.
- A11. The audit procedures described in paragraphs A14-A25 below may be used as risk assessment procedures, tests of controls or substantive procedures, depending on the context in which they are applied by the auditor. As explained in ISA 330, audit evidence obtained from previous audits may, in certain circumstances, provide appropriate audit evidence where the auditor performs audit procedures to establish its continuing relevance.¹⁹
- A12. The nature and timing of the audit procedures to be used may be affected by the fact that some of the accounting data and other information may be available only in electronic form or only at certain points or periods in time. For example, source documents, such as purchase orders and invoices, may exist only in electronic form when an entity uses electronic commerce, or may be discarded after scanning when an entity uses image processing systems to facilitate storage and reference.
- A13. Certain electronic information may not be retrievable after a specified period of time, for example, if files are changed and if backup files do not exist. Accordingly, the auditor may find it necessary as a result of an entity's data retention policies to request retention of some information for the auditor's review or to perform audit procedures at a time when the information is available.

¹⁹ ISA 330, paragraph A35.

Inspection

- A14. Inspection involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production. An example of inspection used as a test of controls is inspection of records for evidence of authorization.
- A15. Some documents represent direct audit evidence of the existence of an asset, for example, a document constituting a financial instrument such as a stock or bond. Inspection of such documents may not necessarily provide audit evidence about ownership or value. In addition, inspecting an executed contract may provide audit evidence relevant to the entity's application of accounting policies, such as revenue recognition.
- A16. Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets. Inspection of individual inventory items may accompany the observation of inventory counting.

Observation

- A17. Observation consists of looking at a process or procedure being performed by others, for example, the auditor's observation of inventory counting by the entity's personnel, or of the performance of control activities. Observation provides audit evidence about the performance of a process or procedure, but is limited to the point in time at which the observation takes place, and by the fact that the act of being observed may affect how the process or procedure is performed. See ISA 501 for further guidance on observation of the counting of inventory.²⁰

External Confirmation

- A18. An external confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium. External confirmation procedures frequently are relevant when addressing assertions associated with certain account balances and their elements. However, external confirmations need not be restricted to account balances only. For example, the auditor may request confirmation of the terms of agreements or transactions an entity has with third parties; the confirmation request may be designed to ask if any modifications have been made to the agreement and, if so, what the relevant details are. External confirmation procedures also are used to obtain audit evidence about the absence of certain conditions, for example, the absence of a "side agreement" that may influence revenue recognition. See ISA 505 for further guidance.²¹

Recalculation

- A19. Recalculation consists of checking the mathematical accuracy of documents or records. Recalculation may be performed manually or electronically.

²⁰ ISA 501, *Audit Evidence—Specific Considerations for Selected Items*

²¹ ISA 505, *External Confirmations*

Reperformance

- A20. Reperformance involves the auditor's independent execution of procedures or controls that were originally performed as part of the entity's internal control.

Analytical Procedures

- A21. Analytical procedures consist of evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount. See ISA 520 for further guidance.

Inquiry

- A22. Inquiry consists of seeking information of knowledgeable persons, both financial and non-financial, within the entity or outside the entity. Inquiry is used extensively throughout the audit in addition to other audit procedures. Inquiries may range from formal written inquiries to informal oral inquiries. Evaluating responses to inquiries is an integral part of the inquiry process.
- A23. Responses to inquiries may provide the auditor with information not previously possessed or with corroborative audit evidence. Alternatively, responses might provide information that differs significantly from other information that the auditor has obtained, for example, information regarding the possibility of management override of controls. In some cases, responses to inquiries provide a basis for the auditor to modify or perform additional audit procedures.
- A24. Although corroboration of evidence obtained through inquiry is often of particular importance, in the case of inquiries about management intent, the information available to support management's intent may be limited. In these cases, understanding management's past history of carrying out its stated intentions, management's stated reasons for choosing a particular course of action, and management's ability to pursue a specific course of action may provide relevant information to corroborate the evidence obtained through inquiry.
- A25. In respect of some matters, the auditor may consider it necessary to obtain written representations from management and, where appropriate, those charged with governance to confirm responses to oral inquiries. See ISA 580 for further guidance.²²

Information to Be Used as Audit Evidence

Relevance and Reliability (Ref: Para. 7)

- A26. As noted in paragraph A1, while audit evidence is primarily obtained from audit procedures performed during the course of the audit, it may also include information obtained from other sources such as, for example, previous audits, in certain circumstances, a firm's quality control procedures for client acceptance and continuance and complying with certain additional responsibilities under law, regulation or relevant ethical requirements (e.g., regarding an entity's non-compliance with laws and regulations). The quality of all audit evidence is affected by the relevance and reliability of the information upon which it is based.

²² ISA 580, *Written Representations*

Relevance

- A27. Relevance deals with the logical connection with, or bearing upon, the purpose of the audit procedure and, where appropriate, the assertion under consideration. The relevance of information to be used as audit evidence may be affected by the direction of testing. For example, if the purpose of an audit procedure is to test for overstatement in the existence or valuation of accounts payable, testing the recorded accounts payable may be a relevant audit procedure. On the other hand, when testing for understatement in the existence or valuation of accounts payable, testing the recorded accounts payable would not be relevant, but testing such information as subsequent disbursements, unpaid invoices, suppliers' statements, and unmatched receiving reports may be relevant.
- A28. A given set of audit procedures may provide audit evidence that is relevant to certain assertions, but not others. For example, inspection of documents related to the collection of receivables after the period end may provide audit evidence regarding existence and valuation, but not necessarily cutoff. Similarly, obtaining audit evidence regarding a particular assertion, for example, the existence of inventory, is not a substitute for obtaining audit evidence regarding another assertion, for example, the valuation of that inventory. On the other hand, audit evidence from different sources or of a different nature may often be relevant to the same assertion.
- A29. Tests of controls are designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level. Designing tests of controls to obtain relevant audit evidence includes identifying conditions (characteristics or attributes) that indicate performance of a control, and deviation conditions which indicate departures from adequate performance. The presence or absence of those conditions can then be tested by the auditor.
- A30. Substantive procedures are designed to detect material misstatements at the assertion level. They comprise tests of details and substantive analytical procedures. Designing substantive procedures includes identifying conditions relevant to the purpose of the test that constitute a misstatement in the relevant assertion.

Reliability

- A31. The reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source and its nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant. Therefore, generalizations about the reliability of various kinds of audit evidence are subject to important exceptions. Even when information to be used as audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability. For example, information obtained from ~~an~~ source independent external source of the entity may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity. While recognizing that exceptions may exist, the following generalizations about the reliability of audit evidence may be useful:
- The reliability of audit evidence is increased when it is obtained from independent sources outside the entity.
 - The reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective.
 - Audit evidence obtained directly by the auditor (for example, observation of the application of a control) is more reliable than audit evidence obtained indirectly or by inference (for example,

inquiry about the application of a control).

- Audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally (for example, a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed).
- Audit evidence provided by original documents is more reliable than audit evidence provided by photocopies or facsimiles, or documents that have been filmed, digitized or otherwise transformed into electronic form, the reliability of which may depend on the controls over their preparation and maintenance.

A32. ISA 520 provides further guidance regarding the reliability of data used for purposes of designing analytical procedures as substantive procedures.²³

A33. ISA 240 deals with circumstances where the auditor has reason to believe that a document may not be authentic, or may have been modified without that modification having been disclosed to the auditor.²⁴

A33a is a conforming amendments to ISA 500 as a result of the approval of ISA 250 (Revised)

A33a. ISA 250 (Revised)²⁵ provides further guidance with respect to the auditor complying with any additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's identified or suspected non-compliance with laws and regulations that may provide further information that is relevant to the auditor's work in accordance with ISAs and evaluating the implications of such non-compliance in relation to other aspects of the audit.

External Information Sources

A33b. The auditor is required by paragraph 7 to consider the relevance and reliability of information obtained from an external information source that is to be used as audit evidence, regardless of whether that information has been used by the entity in preparing the financial statements or obtained by the auditor. For information obtained from an external information source, that consideration may, in certain cases, include audit evidence about the external information source or the preparation of the information by the external information source, obtained through designing and performing further audit procedures in accordance with ISA 330 or, where applicable, ISA 540 (Revised).²⁶

A33c. Obtaining an understanding of why management or, when applicable, a management's expert uses an external information source, and how the relevance and reliability of the information was considered (including its accuracy and completeness), may help to inform the auditor's consideration of the relevance and reliability of that information.

A33d. The following factors may be important when considering the relevance and reliability of information obtained from an external information source, including its accuracy and completeness, taking into account that some of these factors may only be relevant when the information has been used by management in preparing the financial statements or has been obtained by the auditor:

²³ ISA 520, paragraph 5(a)

²⁴ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraph 13

²⁵ ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraph 9

²⁶ ISA 540 (Revised), *Auditing Accounting Estimates and Disclosures*

- The nature and authority of the external information source. For example, a central bank or government statistics office with a legislative mandate to provide industry information to the public is likely to be an authority for certain types of information;
- The ability to influence the information obtained, through relationships between the entity and the information source;
- The competence and reputation of the external information source with respect to the information, including whether, in the auditor's professional judgment, the information is routinely provided by a source with a track record of providing reliable information;
- Past experience of the auditor with the reliability of the information provided by the external information source;
- Evidence of general market acceptance by users of the relevance and/or reliability of information from an external information source for a similar purpose to that for which the information has been used by management or the auditor;
- Whether the entity has in place controls to address the relevance and reliability of the information obtained and used;
- Whether the external information source accumulates overall market information or engages directly in "setting" market transactions;
- Whether the information is suitable for use in the manner in which it is being used and, if applicable, was developed taking into account the applicable financial reporting framework;
- Alternative information that may contradict the information used;
- The nature and extent of disclaimers or other restrictive language relating to the information obtained;
- Information about the methods used in preparing the information, how the methods are being applied including, where applicable, how models have been used in such application, and the controls over the methods; and
- When available, information relevant to considering the appropriateness of assumptions and other data applied by the external information sources in developing the information obtained.

A33e. The nature and extent of the auditor's consideration takes into account the assessed risks of material misstatement at the assertion level to which the use of the external information is relevant, the degree to which the use of that information is relevant to the reasons for the assessed risks of material misstatement and the possibility that the information from the external information source may not be reliable (for example, whether it is from a credible source). Based on the auditor's consideration of the matters described in paragraph A33B, the auditor may determine that further understanding of the entity and its environment, including its internal control, is needed, in accordance with ISA 315, or that further audit procedures, in accordance with ISA 330²⁷, and ISA 540 (Revised)²⁸ when applicable, are appropriate in the circumstances, to respond to the assessed risks of material misstatement related to the use of information from an external information source. Such procedures may include:

²⁷ ISA 330, paragraph 6

²⁸ ISA 540 (Revised), paragraph 29

- Performing a comparison of information obtained from the external information source with information obtained from an alternative independent information source.
- When relevant to considering management's use of an external information source, obtaining an understanding of controls management has in place to consider the reliability of the information from external information sources, and potentially testing the operating effectiveness of such controls.
- Performing procedures to obtain information from the external information source to understand its processes, techniques, and assumptions, for the purposes of identifying, understanding and, when relevant, testing the operating effectiveness of its controls.

A33f. In some situations, there may be only one provider of certain information, for example, information from a central bank or government, such as an inflation rate, or a single recognized industry body. In such cases, the auditor's determination of the nature and extent of audit procedures that may be appropriate in the circumstances is influenced by the nature and credibility of the source of the information, the assessed risks of material misstatement to which that external information is relevant, and the degree to which the use of that information is relevant to the reasons for the assessed risk of material misstatement. For example, when the information is from a credible authoritative source, the extent of the auditor's further audit procedures may be less extensive, such as corroborating the information to the source's website or published information. In other cases, if a source is not assessed as credible, the auditor may determine that more extensive procedures are appropriate and, in the absence of any alternative independent information source against which to compare, may consider whether performing procedures to obtain information from the external information source, when practical, is appropriate in order to obtain sufficient appropriate audit evidence.

A33g. When the auditor does not have a sufficient basis with which to consider the relevance and reliability of information from an external information source, the auditor may have a limitation on scope if sufficient appropriate audit evidence cannot be obtained through alternative procedures. Any imposed limitation on scope is evaluated in accordance with the requirements of ISA 705 (Revised).²⁹

Reliability of Information Produced by a Management's Expert (Ref: Para. 8)

- A34. The preparation of an entity's financial statements may require expertise in a field other than accounting or auditing, such as actuarial calculations, valuations, or engineering data. The entity may employ or engage experts in these fields to obtain the needed expertise to prepare the financial statements. Failure to do so when such expertise is necessary increases the risks of material misstatement.
- A35. When information to be used as audit evidence has been prepared using the work of a management's expert, the requirement in paragraph 8 of this ISA applies. For example, an individual or organization may possess expertise in the application of models to estimate the fair value of securities for which there is no observable market. If the individual or organization applies that expertise in making an estimate which the entity uses in preparing its financial statements, the individual or organization is a management's expert and paragraph 8 applies. If, on the other hand, that individual or organization merely provides price data regarding private transactions not otherwise available to the entity which the entity uses in its own estimation methods, such information, if used as audit evidence, is subject

²⁹ ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*, Paragraph 13

to paragraph 7 of this ISA, ~~but is being~~ information from an external information source and not the use of a management's expert by the entity.

A36. The nature, timing and extent of audit procedures in relation to the requirement in paragraph 8 of this ISA, may be affected by such matters as:

- The nature and complexity of the matter to which the management's expert relates.
- The risks of material misstatement in the matter.
- The availability of alternative sources of audit evidence.
- The nature, scope and objectives of the management's expert's work.
- Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services.
- The extent to which management can exercise control or influence over the work of the management's expert.
- Whether the management's expert is subject to technical performance standards or other professional or industry requirements.
- The nature and extent of any controls within the entity over the management's expert's work.
- The auditor's knowledge and experience of the management's expert's field of expertise.
- The auditor's previous experience of the work of that expert.

The Competence, Capabilities and Objectivity of a Management's Expert (Ref: Para. 8(a))

A37. Competence relates to the nature and level of expertise of the management's expert. Capability relates the ability of the management's expert to exercise that competence in the circumstances. Factors that influence capability may include, for example, geographic location, and the availability of time and resources. Objectivity relates to the possible effects that bias, conflict of interest or the influence of others may have on the professional or business judgment of the management's expert. The competence, capabilities and objectivity of a management's expert, and any controls within the entity over that expert's work, are important factors in relation to the reliability of any information produced by a management's expert.

A38. Information regarding the competence, capabilities and objectivity of a management's expert may come from a variety of sources, such as:

- Personal experience with previous work of that expert.
- Discussions with that expert.
- Discussions with others who are familiar with that expert's work.
- Knowledge of that expert's qualifications, membership of a professional body or industry association, license to practice, or other forms of external recognition.
- Published papers or books written by that expert.
- An auditor's expert, if any, who assists the auditor in obtaining sufficient appropriate audit evidence with respect to information produced by the management's expert.

A39. Matters relevant to evaluating the competence, capabilities and objectivity of a management's expert include whether that expert's work is subject to technical performance standards or other professional or industry requirements, for example, ethical standards and other membership requirements of a professional body or industry association, accreditation standards of a licensing body, or requirements imposed by law or regulation.

A40. Other matters that may be relevant include:

- The relevance of the management's expert's competence to the matter for which that expert's work will be used, including any areas of specialty within that expert's field. For example, a particular actuary may specialize in property and casualty insurance, but have limited expertise regarding pension calculations.
- The management's expert's competence with respect to relevant accounting requirements, for example, knowledge of assumptions and methods, including models where applicable, that are consistent with the applicable financial reporting framework.
- Whether unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures indicate that it may be necessary to reconsider the initial evaluation of the competence, capabilities and objectivity of the management's expert as the audit progresses.

A41. A broad range of circumstances may threaten objectivity, for example, self-interest threats, advocacy threats, familiarity threats, self-review threats and intimidation threats. Safeguards may reduce such threats, and may be created either by external structures (for example, the management's expert's profession, legislation or regulation), or by the management's expert's work environment (for example, quality control policies and procedures).

A42. Although safeguards cannot eliminate all threats to a management's expert's objectivity, threats such as intimidation threats may be of less significance to an expert engaged by the entity than to an expert employed by the entity, and the effectiveness of safeguards such as quality control policies and procedures may be greater. Because the threat to objectivity created by being an employee of the entity will always be present, an expert employed by the entity cannot ordinarily be regarded as being more likely to be objective than other employees of the entity.

A43. When evaluating the objectivity of an expert engaged by the entity, it may be relevant to discuss with management and that expert any interests and relationships that may create threats to the expert's objectivity, and any applicable safeguards, including any professional requirements that apply to the expert; and to evaluate whether the safeguards are adequate. Interests and relationships creating threats may include:

- Financial interests.
- Business and personal relationships.
- Provision of other services.

Obtaining an Understanding of the Work of the Management's Expert (Ref: Para. 8(b))

A44. An understanding of the work of the management's expert includes an understanding of the relevant field of expertise. An understanding of the relevant field of expertise may be obtained in conjunction with the auditor's determination of whether the auditor has the expertise to evaluate the work of the

management's expert, or whether the auditor needs an auditor's expert for this purpose.³⁰

A45. Aspects of the management's expert's field relevant to the auditor's understanding may include:

- Whether that expert's field has areas of specialty within it that are relevant to the audit.
- Whether any professional or other standards, and regulatory or legal requirements apply.
- What assumptions and methods are used by the management's expert, and whether they are generally accepted within that expert's field and appropriate for financial reporting purposes.
- The nature of internal and external data or information the management's expert uses.

A46. In the case of a management's expert engaged by the entity, there will ordinarily be an engagement letter or other written form of agreement between the entity and that expert. Evaluating that agreement when obtaining an understanding of the work of the management's expert may assist the auditor in determining the appropriateness of the following for the auditor's purposes:

- The nature, scope and objectives of that expert's work;
- The respective roles and responsibilities of management and that expert; and
- The nature, timing and extent of communication between management and that expert, including the form of any report to be provided by that expert.

A47. In the case of a management's expert employed by the entity, it is less likely there will be a written agreement of this kind. Inquiry of the expert and other members of management may be the most appropriate way for the auditor to obtain the necessary understanding

Evaluating the Appropriateness of the Management's Expert's Work (Ref: Para. 8(c))

A48. Considerations when evaluating the appropriateness of the management's expert's work as audit evidence for the relevant assertion may include:

- The relevance and reasonableness of that expert's findings or conclusions, their consistency with other audit evidence, and whether they have been appropriately reflected in the financial statements;
- If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods; ~~and~~
- If that expert's work involves significant use of source data the relevance, completeness, and accuracy of that source data; and
- If that expert's work involves the use of information from an external information source, the relevance and reliability of that information.

Information Produced by the Entity and Used for the Auditor's Purposes (Ref: Para. 9(a)–(b))

A49. In order for the auditor to obtain reliable audit evidence, information produced by the entity that is used for performing audit procedures needs to be sufficiently complete and accurate. For example, the effectiveness of auditing revenue by applying standard prices to records of sales volume is affected by the accuracy of the price information and the completeness and accuracy of the sales

³⁰ ISA 620, ~~Using the Work of an Auditor's Expert~~, paragraph 7

volume data. Similarly, if the auditor intends to test a population (for example, payments) for a certain characteristic (for example, authorization), the results of the test will be less reliable if the population from which items are selected for testing is not complete.

- A50. Obtaining audit evidence about the accuracy and completeness of such information may be performed concurrently with the actual audit procedure applied to the information when obtaining such audit evidence is an integral part of the audit procedure itself. In other situations, the auditor may have obtained audit evidence of the accuracy and completeness of such information by testing controls over the preparation and maintenance of the information. In some situations, however, the auditor may determine that additional audit procedures are needed.
- A51. In some cases, the auditor may intend to use information produced by the entity for other audit purposes. For example, the auditor may intend to make use of the entity's performance measures for the purpose of analytical procedures, or to make use of the entity's information produced for monitoring activities, such as reports of the internal audit function. In such cases, the appropriateness of the audit evidence obtained is affected by whether the information is sufficiently precise or detailed for the auditor's purposes. For example, performance measures used by management may not be precise enough to detect material misstatements.

Selecting Items for Testing to Obtain Audit Evidence (Ref: Para. 10)

- A52. An effective test provides appropriate audit evidence to an extent that, taken with other audit evidence obtained or to be obtained, will be sufficient for the auditor's purposes. In selecting items for testing, the auditor is required by paragraph 7 to determine the relevance and reliability of information to be used as audit evidence; the other aspect of effectiveness (sufficiency) is an important consideration in selecting items to test. The means available to the auditor for selecting items for testing are:
- (a) Selecting all items (100% examination);
 - (b) Selecting specific items; and
 - (c) Audit sampling.

The application of any one or combination of these means may be appropriate depending on the particular circumstances, for example, the risks of material misstatement related to the assertion being tested, and the practicality and efficiency of the different means.

Selecting All Items

- A53. The auditor may decide that it will be most appropriate to examine the entire population of items that make up a class of transactions or account balance (or a stratum within that population). 100% examination is unlikely in the case of tests of controls; however, it is more common for tests of details. 100% examination may be appropriate when, for example:
- The population constitutes a small number of large value items;
 - There is a significant risk and other means do not provide sufficient appropriate audit evidence;
or
 - The repetitive nature of a calculation or other process performed automatically by an information system makes a 100% examination cost effective.

Selecting Specific Items

A54. The auditor may decide to select specific items from a population. In making this decision, factors that may be relevant include the auditor's understanding of the entity, the assessed risks of material misstatement, and the characteristics of the population being tested. The judgmental selection of specific items is subject to non-sampling risk. Specific items selected may include:

- *High value or key items.* The auditor may decide to select specific items within a population because they are of high value, or exhibit some other characteristic, for example, items that are suspicious, unusual, particularly risk-prone or that have a history of error.
- *All items over a certain amount.* The auditor may decide to examine items whose recorded values exceed a certain amount so as to verify a large proportion of the total amount of a class of transactions or account balance.
- *Items to obtain information.* The auditor may examine items to obtain information about matters such as the nature of the entity, or the nature of transactions.

A55. While selective examination of specific items from a class of transactions or account balance will often be an efficient means of obtaining audit evidence, it does not constitute audit sampling. The results of audit procedures applied to items selected in this way cannot be projected to the entire population; accordingly, selective examination of specific items does not provide audit evidence concerning the remainder of the population.

Audit Sampling

A56. Audit sampling is designed to enable conclusions to be drawn about an entire population on the basis of testing a sample drawn from it. Audit sampling is discussed in ISA 530.³¹

Inconsistency in, or Doubts over Reliability of, Audit Evidence (Ref: Para. 11)

A57. Obtaining audit evidence from different sources or of a different nature may indicate that an individual item of audit evidence is not reliable, such as when audit evidence obtained from one source is inconsistent with that obtained from another. This may be the case when, for example, responses to inquiries of management, internal auditors, and others are inconsistent, or when responses to inquiries of those charged with governance made to corroborate the responses to inquiries of management are inconsistent with the response by management. ISA 230 includes a specific documentation requirement if the auditor identified information that is inconsistent with the auditor's final conclusion regarding a significant matter.³²

³¹ ISA 530, *Audit Sampling*

³² ISA 230, *Audit Documentation*, paragraph 11

ISA 580, *Written Representations*

Appendix 1

(Ref: Para. 2)

List of ISAs Containing Requirements for Written Representations

This appendix identifies paragraphs in other ISAs that require subject-matter specific written representations. The list is not a substitute for considering the requirements and related application and other explanatory material in ISAs.

- ISA 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements – paragraph 39
- ISA 250, Consideration of Laws and Regulations in an Audit of Financial Statements – paragraph 16
- ISA 450, Evaluation of Misstatements Identified during the Audit – paragraph 14
- ISA 501, Audit Evidence—Specific Considerations for Selected Items – paragraph 12
- ISA 540 (Revised), Auditing Accounting Estimates, ~~Including Fair Value Accounting Estimates~~, and Related Disclosures – paragraph ~~22~~35
- ISA 550, Related Parties – paragraph 26
- ISA 560, Subsequent Events – paragraph 9
- ISA 570 (Revised), Going Concern – paragraph 16(e)
- ISA 710, Comparative Information—Corresponding Figures and Comparative Financial Statements – paragraph 9
- ISA 720 (Revised), The Auditor's Responsibilities Relating to Other Information – paragraph 13(c)

Appendix 2

(Ref: Para. A21)

Illustrative Representation Letter

The following illustrative letter includes written representations that are required by this and other ISAs. It is assumed in this illustration that the applicable financial reporting framework is International Financial Reporting Standards; the requirement of ISA 570 (Revised)³³ to obtain a written representation is not relevant; and that there are no exceptions to the requested written representations. If there were exceptions, the representations would need to be modified to reflect the exceptions.

(Entity Letterhead)

(To Auditor)

(Date)

This representation letter is provided in connection with your audit of the financial statements of ABC Company for the year ended December 31, 20XX³⁴ for the purpose of expressing an opinion as to whether the financial statements are presented fairly, in all material respects, (or *give a true and fair view*) in accordance with International Financial Reporting Standards.

We confirm that (, *to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves*):

Financial Statements

- We have fulfilled our responsibilities, as set out in the terms of the audit engagement dated [insert date], for the preparation of the financial statements in accordance with International Financial Reporting Standards; in particular the financial statements are fairly presented (or give a true and fair view) in accordance therewith.
- ~~Significant~~ The methods, the data, and the significant assumptions used in making accounting estimates, including those measured at fair value, and their related disclosures are appropriate to achieve recognition, measurement or disclosure that is reasonable in the context of the applicable financial reporting framework. (ISA 540 (Revised))

Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of International Financial Reporting Standards. (ISA 550)

³³ ISA 570 (Revised), *Going Concern*

³⁴ Where the auditor reports on more than one period, the auditor adjusts the date so that the letter pertains to all periods covered by the auditor's report.

ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

Requirements

...

Forming an Opinion on the Financial Statements

13. In particular, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework:
- (a) The financial statements appropriately disclose the significant accounting policies selected and applied. In making this evaluation, the auditor shall consider the relevance of the accounting policies to the entity, and whether they have been presented in an understandable manner; (Ref: Para. A4)
 - (b) The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;
 - (c) The accounting estimates and related disclosures made by management are reasonable;
 - (d) The information presented in the financial statements is relevant, reliable, comparable, and understandable. In making this evaluation, the auditor shall consider whether:
 - The information that should have been included has been included, and whether such information is appropriately classified, aggregated or disaggregated, and characterized.
 - The overall presentation of the financial statements has been undermined by including information that is not relevant or that obscures a proper understanding of the matters disclosed. (Ref: Para. A5)
 - (e) The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and (Ref: Para. A6)
 - (f) The terminology used in the financial statements, including the title of each financial statement, is appropriate.

ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

Requirements

...

Determining Key Audit Matters

9. The auditor shall determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following: (Ref: Para. A9–A18)
- (a) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with ISA 315 (Revised). (Ref: Para. A19–A22)
 - (b) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that ~~have been identified as having~~ are subject to a high degree of estimation uncertainty. (Ref: Para. A23–A24)
 - (c) The effect on the audit of significant events or transactions that occurred during the period. (Ref: Para. A25–A26)

...

Application and Other Explanatory Material

Significant Auditor Judgments Relating to Areas in the Financial Statements that Involved Significant Management Judgment, Including Accounting Estimates that ~~Have Been Identified as Having~~ Are Subject to a High Degree of Estimation Uncertainty (Ref: Para. 9(b))

- A23. ISA 260 (Revised) requires the auditor to communicate with those charged with governance the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures.³⁵ In many cases, this relates to critical accounting estimates and related disclosures, which are likely to be areas of significant auditor attention, and also may be identified as significant risks.
- A24. However, users of the financial statements have highlighted their interest in accounting estimates that ~~have been identified as having~~ are subject to a high degree of estimation uncertainty (see ~~in accordance with~~ ISA 540 (Revised)³⁶) that may have not been determined to be significant risks. Among other things, such estimates are highly dependent on management judgment and are often the most complex areas of the financial statements, and may require the involvement of both a management's expert and an auditor's expert. Users have also highlighted that accounting policies that have a significant effect on the financial statements (and significant changes to those policies) are relevant to their understanding of the financial statements, especially in circumstances where an entity's practices are not consistent with others in its industry.

³⁵ ISA 260 (Revised), paragraph 16(a)

³⁶ See paragraphs 150–14 of ISA 540 (Revised), *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*.

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 7.1
Meeting date: 5 September 2018
Subject: NZAuASB Strategic Action Plan
Date: 22 August 2018
Prepared by: Peyman Momenan

☒ **Action Required**

☐ **For Information Purposes Only**

Agenda Item Objectives

For the Board to:

- CONSIDER the proposed responses to the findings of the NZAuASB research on assurance needs of small charities; and
- APPROVE the recommended next steps.

Background

1. In 2017, the final research report and findings of the NZAuASB on [assurance needs of funders of small registered charities](#) was issued. A summary of the research findings is included in the Agenda item 7.2.
2. One of the report's recommendations was to explore the viability of the development of a new engagement standard and/or guidance for small entities as an alternative to an audit or review. This Agenda item addresses that recommendation.
3. Agenda item 7.2 includes two general directions that we propose can be adopted in relation to the recommendation. Agenda item 7.2 further includes possible options under each direction and the proposed next steps.

Matters to consider

4. We request feedback from the Board on:
 - The general directions discussed in the issues paper at Agenda item 7.2. Are there any other directions that needs to be considered?
 - The options included under each direction. Are there any other options that should be included?

5. Does the Board agree with the proposed next steps for the project?

Material Presented

Agenda item 7.1	Board Meeting Summary Paper
Agenda item 7.2	Issue paper

Background and objective of this Agenda item

In 2017 the NZAuASB undertook a research project to understand:

- What drives small¹ charities to obtain assurance over their financial statements?
- Are the needs of funders, such as philanthropic funding organisations (PFOs) and government agencies) appropriately addressed by the assurance engagement?

The key findings of the research were as follows.

- Most small charities have their financial statements audited or reviewed because their founding documents require them to do so, not because PFOs demand assurance over small charities annual reports.
- While the requirement for an assurance engagement included in the small charities may be a legacy of perceived best practices and a legacy from the past, those charged with governance of these small charities consider it prudent to obtain some form of external scrutiny over their financial operations and reports. However, a perceived lack of value for money of audit and review engagements is a significant deterrent for small charities to use these assurance products. As small charities are very likely to spend a significant portion of their limited financial resources to procure the services of chartered accountants in preparing their year-end annual reports, getting value for money from an assurance engagement becomes even more important for small charities.
- Both government agencies and PFOs have significant information needs for assessing the capabilities of small charities. Most of the information they require is not included in the small charities' annual reports. An audit report may be inappropriately relied on by the funding organisation as a stamp of approval for "financial management capability".

The NZAuASB intended to use the results of the research to decide whether a new simple assurance engagement should be developed for small charities. The outcome of the research indicates that such decision can consider two different directions as follows.

- Direction 1: developing a cheaper alternative for an audit or a review of financial statements.
- Direction 2: delivering more value from an audit engagement by extending its scope to include opinion/comment on entity's financial management capabilities.

It should be noted that the research found that funders demand information that is largely outside the scope of information included in the financial statements of small registered charities. However, unlike financial reporting, this information does not have any statutory, or otherwise generally accepted, basis for preparation at present. Consequently, while there is a significant potential demand for assurance engagements in this space, the NZAuASB's mandate does not enable us to progress in that direction unless the outlook of non-financial reporting by charities is significantly changed.

¹ Those charities with annual expenditure between \$125k and \$500k with no statutory requirement for an audit or a review.

Direction 1: developing a cheaper alternative for an audit or a review of financial statements.

There is demand from members (but not from external funders) of the small charities for independent scrutiny over the charities' financial affairs and their financial reports. However, as many small charities spend a significant portion of their limited financial resources on preparing their financial statements (e.g. procure services of professional accountants to prepare annual reports), they find the costs of an audit or a review unaffordable.

The demand for an engagement that is effectively a "cheaper audit" (in that it provides confidence in the financial statements but costs less than an audit engagement) is neither new nor unique to New Zealand. For example, in recognition to such demand, the Charities Commission for England and Wales have developed "[Independent Examination of charity accounts](#)".

As well as a lower bar for who can carry out an Independent Examination², the other major differences between an audit and an IE lie in the level of scrutiny and the nature of the report:

- an independent examiner does not scrutinise a charity's accounts to the same level as an audit (although the Charity Commission's Directions still take the examiner through a 12-stage process)
- an independent examiner writes a report which gives negative assurance ('no matter has come to my attention ...') rather than positive assurance (a 'true and fair' view).

In essence, an IE is a light review engagement allowed to be performed by anyone who is deemed adequately knowledgeable of financial and accounting matters (including members of the charity). The expectation of an IE being cheaper than an audit is due to:

- more flexibility with who can be appointed as an Independent Examiner, increasing the likelihood of a charity being able to appoint a volunteer (e.g. a member that is not involved in day to day running or governance of the charity) or someone with cheaper rates than a professional accountant as IE.
- Reduced work effort compared to an engagement undertaken in accordance with international auditing or review standards (including no need to comply with quality control or ethical requirements).

A different concept that has been developing for some time is the "differential audit standard". An example of a differential audit standard that have received global attention in the last few years is the Nordic countries project to develop a separate standard for audits of small entities ("the Nordic standard" or "SASE"). The IAASB [described](#) the draft standard as follows.

² The Trustees of a charity seeking an Independent Examination must be confident that the person conducting the IE is independent and has the requisite ability and the practical experience to carry out a competent examination of the accounts. In England and Wales, an Independent Examiner does not have to have a formal qualification, although the Charity Commission recommends that:

- they are a qualified accountant - or are 'an individual with similar qualifications in charity finance at an appropriate level' - for accounts in the £100,000 to £250,000 per year range (or where the charity's gross assets are over £1m)
- and that if the accounts are to be prepared on an accruals basis under this threshold, then the requisite understanding of the relevant accounting principles is demonstrated.
- once the upper limit for IE in England and Wales has risen to £500,000, anyone examining accounts over £250,000 will have to have a professional qualification from a prescribed list, which includes the Association of Charity Independent Examiners (ACIE).

“ the draft SASE can at best be described as a very short summary of the ISA requirements that are most likely relevant for a simple small audit. The draft SASE is a collection of excerpts from various ISA requirements, and in limited cases from objectives, definitions, application material and appendices (important elements of the ISAs)”

The Nordic standard is still in draft stage. However, the IAASB has commented that “the proposed SASE is very different than ISAs and audits performed under the SASE could differ significantly from an ISA audit in terms of audit quality”. The feedback provided on the Nordic standard in the IAASB forum for SMPs held in Paris in 2017 also showed a lack of support for a differential auditing standard (such as the Nordic standard).

Agreed upon procedures have been discussed as another alternative for an audit or a review for an assurance engagement over a small charities financial statements, with some New Zealand firms reporting to the NZAuASB that they already use AUPs in this space.

Finally, as noted in the research findings, professional accountants already play a significant role in assisting small charities with preparation of their year-end accounts. For example, the research found that a considerable number of small charities have had their financial statements compiled by professional accountants. There is therefore merit in investigating the possibility of a hybrid professional engagement whereby additional efficiency (and therefore lower costs) are potentially achieved by combining roles currently separated.

Another point to consider is the developments in cloud-based accounting software. For example, the Xero accounting software is currently offering an “[assurance dashboard](#)” that allows specific users (such as an external auditor) to view (amongst other things) the integrity of transactions within a system. There is potential in exploring how use of technology can help reduce the cost of audit or review for engagements on small entities. This may be achieved by incorporating more automated internal controls into the system as well as developing Data Analytics tools that can be helpful for auditors. The fact that many small charities use these cloud-based accounting software increases the potential for developing audit specific features to be embedded into the software and/or application programming interfaces (APIs) to be attached to the software.

It must be noted that an alternative for a cheaper assurance engagement can be how (and who) pays the costs of an audit or a review engagement. For example, a New Zealand professional accounting firm has registered itself as a not- for- profit entity and provides audit or review engagements at significantly discounted prices to registered charities. It funds the cost of its services by receiving funding from PFOs. The Independent Examiner regime in the UK’s main attractiveness is that it makes it easier for small charities to appoint volunteers instead of paying professionals. So, there is a risk that no level of cheaper will be cheap enough if the burden of the cost is to be shouldered by the small charity, and audits or reviews may not be deemed unaffordable where they are paid by others (e.g. specific funding was allocated for annual audits as part of a government service agreement).

Finally, a way to improve the deemed value of a conventional audit or review engagement is to modify the outputs of the engagements in a way that delivers more value for money. However, such an approach is unlikely to be feasible without some level of change in what information small charities provide to their funders. Therefore, any potential for delivering more from an audit or a review engagement is considered under Direction 2 on the following page.

Direction 2: delivering more value from an audit engagement by extending its scope to include opinion/comment on an entity's financial management capabilities.

The research findings indicate the funders of small charities see a greater need for assurance on information that is not included in the small charities' financial statements. For example, both government and PFOs would want to evaluate the "financial management capabilities" of their applicants to ensure that there is a low risk of funds being misappropriated or mismanaged. The funders indicated strong demand for any engagement that can help them in forming their views about "financial management capabilities" of their applicants.

Another finding of this research was that small charities provide the same information (especially information that can be generally categorised as "background information") to multiple stakeholders. However, lack of a method for preparing this information in a "general purpose" manner means that charities will need to produce this information multiple times for each funder, who then needs to establish its credibility. If it was possible for such information to be prepared and/or shared in a different manner (e.g. if there is a single platform where a small charity can upload all the background information that all external stakeholders can use for their own purposes)³, then both small charities and their funders would demand an assurance product to enhance the credibility of that information (e.g. an independent assurance practitioner validates the information for all interested parties).

However, responding to these assurance needs require developments that are outside the mandate and/or control of the NZAuASB. From an assurance standard-setting perspective, those needed developments can be best described as developing suitable criteria for the engagement. For example, addressing the funders' assurance needs in relation to small charities "financial management capability" requires suitable criteria that is not readily available (or widely adopted) at present.

Developing (or adopting) such criteria is not necessarily a highly demanding or technically infeasible task. For example, Crown agencies responsible for social sector purchasing (MSD, MOH, MOE, Ministry of Justice, the Department of Corrections and Te Puni Kōkiri) have already agreed on a standard for "Financial Management and Systems" that can be a foundation for suitable criteria. Similarly, the Charities Commission for England and Wales have published [guidance on internal financial controls for charities](#) that can be used to evaluate some basic financial management capabilities. As an audit of financial statements already involves obtaining an appropriate level of understanding of an entity's internal controls relevant to audit, there is a potential to deliver more value from an audit by also enabling the auditor to provide confidence that an entity's internal financial controls are consistent with an accepted best-practice or standard. Similarly, the work effort of an audit engagement involves verifying information that funders require as "background" information. There is potential to leverage that work effort to help funders and small charities to reduce duplication for the effort involved in collection and verification of that information. Again, this is feasible (e.g. should the Charities Register be upgraded to enable a single point for updated and independently verified background information).

Nevertheless, it will not be feasible to develop an assurance engagement to enhance confidence in those underlying subject matters without suitable criteria being established first. This requires the

³ The demand for a more innovative way of sharing information to reduce the administrative burdens of charities and their funders is also evidenced in the feedback provided by community and voluntary sector organisations to the Department of Internal Affairs in a series of workshops held in June and July 2017. See the full report [here](#).

NZAASB to work together with other agencies (especially the Charities Services and professional accounting bodies such as the CAANZ) to be able to pursue this option.

Summary of options under each direction

Options under direction 1

1. Exploring developing an assurance engagement specifically for small charities (similar to the Independent Examiner product in the UK).
2. Exploring the “differential auditing” concept.
3. Exploring the concept of a hybrid engagement where a professional accountant can assume a broader responsibility in relation to the small charities financial reporting (e.g. an engagement that encompasses both a compilation and a review engagement).
4. Exploring how the use of technology can increase efficiency and effectiveness of small audits and therefore reduce its cost. This would require working closely with auditors of small charities, professional accounting bodies and the developer of accounting software.
5. Exploring how non-assurance services (such as AUPs) can be utilised in this space.

Options under direction 2:

1. Exploring the concept of enabling more valuable output from an audit engagement (e.g. commentary on “financial management capabilities” or opinion on “internal financial controls” by leveraging the work an auditor is required to do over understanding internal controls systems). This would require working closely with the Charities Services, Crown agencies responsible for social sector purchasing and PFOs to develop a minimum standard for “financial management capabilities” or “internal financial controls”.
2. Exploring how new assurance concepts can facilitate the current initiatives to enhance information sharing between small charities and their external stakeholders (such as funders) and reducing duplications. This would require working closely with small charities, PFOs and sector regulators.
3. Exploring if assurance practitioners can enhance the credibility of information publicly available about a charity (e.g. on the Charities Register).

What next?

We consider any work in this area will provide valuable input to the IAASB’s project on SMEs.

We recommend:

- appointing a working group (“think tank”) to consider the various options and oversee the development of the project. The working group should include representatives from Charities Services, PFOs, SMPs, and any other relevant organisation or these representatives could be consulted separately as a Consultative Group.
- the working group to recommend a preferred option (based on the direction and options approved by the Board).
- A project plan to be presented to the Board for its consideration and approval at the December 2018 meeting.

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 8.1
Meeting date: 5 September 2018
Subject: Prospective Financial Information
Date: 14 August 2018
Prepared by: Sharon Walker

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Objectives

1. The objective of this agenda item is:
 - to CONSIDER and APPROVE the revised project timetable.

Background

2. At its October 2017 meeting, the Board approved a project proposal to develop a standard for the performance of, and reporting on, assurance over prospective financial information.
3. Preliminary issues were considered at the Board's February 2018 meeting, including necessary changes to the approved project timetable as a consequence to the issues identified.
4. Since that meeting, conflicting priorities with other projects have led to further delays in the progress of the proposed standard.
5. The project timetable has been updated for the Board's consideration.

Matters for Consideration

6. The Board is asked to CONSIDER and APPROVE the revised project timetable.

Material Presented

8.1	Board meeting summary paper
8.2	Project plan (revised timetable)

Project Plan

Project Title:	Prospective Financial Information
Project Objective(s):	Develop a standard for performance of and reporting on prospective financial information
Priority:	Medium
Issue/Reason:	No domestic standard; International standard out of date
Date Prepared:	11 October 2017
Date Approved:	25 October 2017
Date Updated: (if applicable)	5 September 2018

Project Objectives

1. To develop a standard for the performance of and reporting on prospective financial information.

Background

2. Local government entities are required to prepare long term plans, on a three yearly cycle, that include prospective financial information covering the 10 year period of the plan. Such prospective financial information is to be audited. Currently, long term plans are audited in accordance with the Auditor General's auditing standards, ISAE (NZ) 3000 (Revised), *Assurance Engagements Other than Audits and Reviews of Historical Financial Information*, and ISAE 3400, *The Examination of Prospective Financial Information*.
3. In addition, firms are increasingly being requested to undertake assurance engagements that include prospective financial information.
4. ISAE 3400 is more than 20 years old and has not been revised in line with the conventions used in ISAE 3000 (Revised) or to reflect the IAASB's clarity drafting conventions. At this time, there are no current plans for the IAASB to revise ISAE 3400.

International

5. International Standard on Assurance Engagements (ISAE) 3400, *The Examination of Prospective Financial Information*, (previously ISA 810), establishes standards and provides guidance on engagements to examine and report on prospective financial information, including examination procedures for best-estimate and hypothetical assumptions. ISAE 3400 predates the IAASB's clarity project and the issue of ISAE 3000 (Revised), *Assurance Engagements Other than Audits and Reviews of Historical Financial Information*.

Australia

6. The AUASB issued Standard on Assurance Engagements (ASAE) 3450, *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information*, in November 2012. ASAE 3450 deals with the responsibilities of the assurance practitioner when undertaking an engagement to report on the responsible party's preparation of financial information related to a corporate fundraising, or if the financial information is prospective, if it is prepared for another purpose. ASAE 3450 builds on the requirements and application material included in either ASAE 3000, *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, or ASRE 2405, *Review of Historical Financial Information Other than a Financial Report*, in an assurance or review engagement respectively.

Risks/Issues

Issues which may impact the drafting of the standard include the following:

7. Harmonisation with the current AUASB standard, ASAE 3450.
8. The scope of ASAE 3450 addresses more than prospective financial information. Consideration needs to be given as to whether the scope of ASAE 3450 is broader than intended by the Board.
9. The ISAE is out of date and needs to be revised. It therefore may not be the best starting point. Given the XRB is a standard taker rather than a standard maker, we suggest starting with ASAE 3450, amending as necessary to reflect the NZ environment.

Action Plan

10. The project will involve the following key steps:
 1. Considering the need for a sub-committee of the Board to develop the draft standard to meet as required.
 2. Developing a reference group (if considered necessary by the Board) to assist with the project by identifying key issues to be addressed and field testing ideas as they develop. The reference group would meet as required. Such reference group would include broad representation.
 3. Develop a first draft of a standard, based on ASAE 3450, amended as necessary to reflect local regulatory conditions and practices.
 4. Further refine the standard following the Board's feedback.
 5. Expose a draft standard.
 6. Obtain and collate comments, and obtain the Board's approval of amendments to address comments.
 7. Final approval obtained from the Board to issue a new standard.
 8. Quality assurance to be conducted prior to issuing.
 9. Release standard with Communique alert and any other explanatory statements as required.
 10. Consider the need for further education sessions once the final standard is released.

Timetable

11. It is anticipated that it will take about 15 months to develop and finalise the standard. Indicative timings are as follows:

Description	Proposed Date
NZAuASB approves project plan at Board meeting	25 October 2017
NZAuASB to consider initial issues to explore.	February 2018
Establishment of a reference group (if needed)	Q1 2018 (to meet as required)
Establishment of a sub-committee of the NZAuASB to assist in developing ideas and recommendations to present to the NZAuASB (if needed)	Q1 2018(to meet as required)
NZAuASB to consider key issues and draft document	April <u>September, December</u> 2018
Approval of NZAuASB exposure draft	June 2018 <u>February 2019</u>
Exposure draft open for comment	<u>Mar – May 2019</u> – Sept 2018
Consideration of submissions	<u>June – July 2019</u> Oct 2018
Read and Approval of final standard	<u>September-October 2019</u> Dec 2018

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO. 9.1
Meeting date: 5 September 2018
Subject: NZ SRE 2410
Date: 20 August 2018
Prepared by: Misha Pieters



Action Required



For Information Purposes Only

Agenda Item Objectives

To:

- AGREE a way forward to maintain the domestic standard NZ SRE 2410, the standard dealing with interim review engagements conducted by the auditor of the entity.

Background

1. The NZAuASB has issued two review engagement standards: ISRE (NZ) 2400 *Review of Historical Financial Statements Performed by an Assurance Practitioner* and NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*.
2. The IAASB has issued ISRE 2410 but has not amended it since 2006 (i.e. it is not in the clarified format). It was for this reason that the NZAuASB agreed to issue a domestic standard to address interim reviews conducted by the auditor of the entity. The NZAuASB based NZ SRE 2410 on an equivalent Australian standard, which is in the clarified format, rather than the older version issued by the IAASB.
3. The matter of how the NZAuASB wishes to maintain this domestic standard has been on the NZAuASB's strategic action plan since the finalisation of the auditor reporting standards where the question arose as to whether the standard should be updated for the auditor reporting amendments. NZ SRE 2410 was issued in 2013 and it may be timely for a post-implementation review of this domestic standard.
4. The AUASB issued a [bulletin](#) expanding on "Auditor review reports - the impact of the new auditor reporting requirements". This bulletin highlighted that the auditor must continue to comply with ASRE 2410 but may (but is not required to) use the auditor reporting format for review reports.
5. The NZAuASB briefly discussed this Bulletin at the time, and there was a view expressed that it may be preferable to promote consistency in practice. The question whether to amend NZ SRE 2410 for conforming amendments made to the ISAs as a result of IESBA's amendments dealing with non-compliance with laws and regulations was also raised.

6. The issues paper explores the issues in more detail and identifies various options. This paper has been shared with the AUASB staff and the AUASB will be considering similar issues. Any actions taken could be completed as a joint project.
7. Staff recommendation is that:
 - a) NZ SRE 2410 should be amended to promote consistency in reporting however should not include KAMs at this stage;
 - b) If NZ SRE 2410 is to be amended, conformity amendments for the NOCLAR project should be incorporated at the same time;
 - c) In order to maintain NZ SRE 2410 (and other domestic standards) going forward, an annual omnibus exposure draft should be prepared to consider the impact of all of the IAASB's amendments (once finalized) on the domestic standards that impact on auditors.
8. The Board is asked for feedback as to which direction is preferred.

Material Presented

Agenda item 9.1	Board Meeting Summary Paper
Agenda item 9.2	Issues paper.

Issues paper

1. The question whether and how to address matters arising as a result of recent changes made to the auditing standards where the auditor is conducting an interim review of the financial statements has arisen. In New Zealand, interim reviews are sometimes conducted for listed entities. Staff have identified various possible ways forward and this issues paper explores options and issues in more detail.

Auditor reporting changes

2. The need to consider whether to revise NZ SRE 2410 arose on completion of the auditor reporting project. Key changes made to the auditor's report included, but were not limited to, the reporting of key audit matters (KAMs). Other changes made included:
 - Re-ordering the report so that the conclusion comes first;
 - Naming the engagement partner in the interim review report;
 - Including an independence statement;
 - Referring to a material uncertainty related to going concern as an "emphasis of matter" or under the heading "Material uncertainty related to going concern".
3. A key reason for making these changes to the auditor's report was to enhance the value of the auditor's report to better meet user needs.
4. The AUASB's bulletin permits the auditor to reorder the report and include elements of the revised auditor reporting requirements, without requiring them to do so. The bulletin stresses the importance of complying with ASRE 2410, which is not prescriptive in terms of the order, etc.
5. In Australia, it is required by law for the engagement partner to include their name on both the auditor's report and the interim review report (this was required before the auditor reporting changes), i.e. it is consistent practice for the engagement partner's name to appear in both the year end and interim review reports. This is not required in New Zealand. On a sample of interim review reports considered by staff, the name of the engagement partner does not appear in the interim review reports.
6. We have requested initial feedback from the big four firms as well as the FMA. Feedback received so far is unanimously opposed to reporting KAMs at the interim review stage, noting that less work is performed in a review therefore KAMs will be less useful, and may be misunderstood given that an audit has not been performed at this stage.
7. Views were mixed on the other changes: one was opposed to doing anything ahead of the IAASB and a few were not concerned about requiring consistency (i.e. consistency or lack

thereof was not considered to be an issue given that there is already variation in audit reports (e.g., some including materiality etc). One was supportive of including all of the other changes mentioned above, on the basis that they are all relevant. Other views were mixed, supporting consistency in the reporting of matters related to going concern but less supportive of the need to include the engagement partner's name.

8. Based on feedback received when conducting research for the joint report on KAMs with the FMA, in our view it is too early to consider whether to extend the reporting of KAMs to review reports. We recommend continuing to monitor the reporting of KAMs and the IAASB's discussions when the post-implementation review of the auditor reporting requirements is performed. We consider that it is too early to move ahead of the IAASB in this space and there have been no calls to suggest that there is a compelling reason to do so.
9. However, we do recommend a consideration of whether the other changes made in the auditor reporting project should be amended in the domestic standard, NZ SRE 2410, at this time. From a user perspective, we consider that a more consistent approach between the year-end the interim review report may enhance the users understanding.
10. Moving the opinion, including the name of the engagement partner and including an independence statement are all possible under the extant requirements of NZ SRE 2410. I.e. if the auditor chose to do so, they would still be complying with the standards issued by the NZAuASB. However, this would be optional (and therefore could be inconsistently done in practice).
11. Indicative feedback from analysts was in favour of reporting the engagement partners' name. We consider that it may be misleading not to include the engagement partner name on the interim review report. If the engagement partner has changed since the year end audit, it could mislead the user to believe that the same engagement partner has performed the interim review. As noted above this is inconsistent with practice in Australia.
12. Indicative and early feedback from users suggested that moving the opinion upfront was useful. We consider that there is merit in requiring the conclusion to move to the top of the interim review report rather than including guidance that permits this. This may drive inconsistent practice in the way in which auditors report and be confusing to users. Whilst this may be inconsistent with a review report which is prepared under ISRE (NZ) 2400 (i.e. for a year end review engagement) such a report will be targeted at a different user group.
13. We consider that independence is just as important for an interim review as it is for the audit. The same independence requirements apply and therefore it would be useful to report this consistently in the review report to avoid any doubt (noting this is for listed entities in New Zealand).

14. The reporting of matters to do with going concern differs under the extant requirements of NZ SRE 2410 with those of the new auditor's report. NZ SRE 2410¹ refers to reporting of an emphasis of matter paragraph (consistent with the older requirements for auditor reporting). In the new auditors report such matters are reported under the heading of "Material uncertainty related to going concern"². To drive consistency in reporting would require a change to the requirements of NZ SRE 2410.
- 15. Does the Board consider that NZ SRE 2410 should be amended to promote consistency in reporting for the auditor reporting changes (other than KAMs) or would guidance be sufficient? Does the Board agree that it is too early to consider reporting KAMs for interim reviews?**

Non-compliance with laws and regulations (NOCLAR) changes

16. In November 2016 the NZAuASB issued amendments to ISA (NZ) 250³. These changes were conforming amendments made to maintain consistency with the NOCLAR framework issued by the IESBA. Conforming amendments were made by the IAASB to ISRE 2400 (Revised), but not to ISRE 2410 (as this standard has not been amended at all by the IAASB).
17. For example, the requirement to communicate the matter to those charged with governance, was amended to include the reference "unless prohibited by law or regulation" in ISRE (NZ) 2400 but no such change has been made to the equivalent paragraph in NZ SRE 2410 (paragraph 31). Additional application material was included in ISRE (NZ) 2400 to clarify that the assurance practitioner may have additional responsibilities under law, regulation and relevant ethical requirements that go beyond ISRE (NZ) 2400 but no such application material has been added to NZ SRE 2410.
18. The question arising is whether the NZAuASB considers that NZ SRE 2410 (a domestic standard that already differs from the IAASB's equivalent standard) should be amended for the NOCLAR amendments. The IAASB has no plans to update ISRE 2410.
19. Possible options identified:
- a. Conduct a comprehensive post-implementation review of NZ SRE 2410 at this stage to identify all possible changes needed to conform with recent amendments made by the IAASB as well as considering other matters arising. This may include the current projects of the IAASB on estimates and risk assessment, noting that the IAASB has not considered the impact of these projects on review

¹ NZ SRE 2410, paragraph 41

² ISA (NZ) 570, *Going Concern*, paragraph 22.

³ ISA (NZ) 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*

engagements but that in the case of NZ SRE 2410, this is conducted by the auditor;

- b. Also consider performing a post-implementation review of ISRE (NZ) 2400;
- c. Limit changes to NZ SRE 2410 to those identified above, related to auditor reporting changes, as these impact on the user and therefore may best serve user needs;
- d. Update NZ SRE 2410 but limit to the NOCLAR changes and the auditor reporting changes as noted above.

20. Staff recommend option (d) if the Board is going to make amendments as noted above. Further research is needed to better understand the extent of use of the review engagement in New Zealand (ISRE (NZ) 2400). To make further amendments to NZ SRE 2410 at this stage may risk getting ahead of the IAASB's thinking on review engagements.

21. Which option does the Board prefer to deal with NOCLAR and any other possible changes to the NZ SRE 2410?

Other projects

22. When NZ SRE 2410 was issued, there was recognition that it had not been updated to take into account all of the issues contemplated by the IAASB when issuing ISRE 2400 (Revised) and that ISRE 2400 (Revised) covered some aspects in more detail. The discussion was that NZ SRE 2410 covered the principles, but not the detail. There was not a huge appetite to perform this work locally given that there was no evidence to suggest that this was a domestic priority. The Board encouraged the IAASB to consider updating ISRE 2410 at that time.

23. The IAASB has proposed changes to ISA 315. NZ SRE 2410⁴ is premised on the basis that the auditor will have an understanding of the entity as required by ISA (NZ) 315 when conducting the interim review but may need to obtain an understanding of internal control as it relates to the preparation of the interim financial statements, as it may differ. These may or may not need some conforming amendments to align to ISA 315 (Revised) when finalised.

24. An initial analysis of NZ SRE 2410 did not raise any need for amendment as a result of changes to ISA 540, but a more detailed analysis may be required if the board wishes to conduct a complete review of the standard.

⁴ NZ SRE 2410, paragraph A9

25. Expected possible proposed changes to the quality control standards by the IAASB may impact on NZ SRE 2410. We note that NZ SRE 2410 differs from ASRE 2410 with respect to a requirement to comply with ISA (NZ) 220 Quality Control. ASRE 2410 is silent on this.

26. There remains a question as to how the Board wishes to maintain NZ SRE 2410 going forward. For example, does the Board consider there is a need to prepare conforming amendments to NZ SRE 2410 as a result of any changes made by the IAASB at the time those changes are made, or should there be periodic reviews of this domestic standard every couple of years to catch up on pervasive changes? Another option is to prepare an annual omnibus amending exposure draft to catch any necessary domestic changes but this will only be able to be prepared once the IAASB has finalised its proposals. If considered to be urgent then this could be prepared sooner than on an annual basis.

27. If the Board considers that the New Zealand changes should be exposed simultaneously with the relevant IAASB exposure draft, this may delay the issue of the international exposure draft in New Zealand but has the benefit of dealing with the issue simultaneously throughout the suite of standards.

28. A similar question will arise once the NZAuASB issues NZ AS 1 *The Audit of Service Performance Information*, and any other domestic standards that impact on the auditor.

29. Does the Board have a view on whether domestic standards that impact on auditors should:

a. Be maintained simultaneously to changes made by the IAASB?

b. Be maintained periodically (i.e update the domestic standards every three to four years) to update them for international standards?

c. Be maintained by way of an annual omnibus amending standard?



NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

DATE: 24 August 2018

TO: Members of the New Zealand Auditing and Assurance Standards Board

FROM: Peyman Momenan

SUBJECT: International Update

Introduction

1. This Update summarises the significant news of the IAASB, other national auditing standards-setting bodies and professional organisations for the Board's information, for July and August 2018.

International Federation of Accountants (IFAC)

1. In August 2018, the IFAC SMP Committee [responded](#) to the IAASB Strategy Survey. The SMPC emphasised that it is important for the IAASB to give greater consideration to matters relating to SMEs and SMPs in all of its activities. For example, the SMPC believes that the IAASB should look closely at root cause analysis behind regulator findings that result in calls for the IAASB to act. If the standards are sound, but non-compliance is the issue, there may be no need for action by the IAASB. Where misunderstanding/ misinterpretation of the standards has led to non-compliance, clarification (e.g. implementation support) could be warranted.
2. The IFAC Professional Accountants in Business (PAIB) Committee has submitted a comment letter in response to the IESBA's consultation paper, Professional Scepticism - Meeting Public Expectations. The PAIB Committee believes strongly professional scepticism is a fundamental ethical obligation applied in the work of all professional accountants including professional accountants in business and is a key distinguishing element of the profession. PAIB strongly supported that professional scepticism (as defined in the IESBA's consultation paper) should be included in the Code.

International Auditing and Assurance Standards Board (IAASB)

3. IAASB Ongoing projects (refer to appendix 1)

International Ethics Standards Board for Accountants (IESBA)

1. IESBA news for the period are all covered in the meeting Agenda items.

Accountancy Europe (AE) (former FEE)

1. About two years after the implementation deadline, FEE presented an [updated state of play of this process in 30 European countries](#), including 28 EU Member States. FEE has further analysed Member States' decisions and visualised the outcomes for the key options regarding:
 - providing non-audit services
 - mandatory audit firm rotation
 - organising public oversight

To provide a better overview and make information easier to understand, information on non-audit services, mandatory audit firm rotation and public oversight is displayed in a more detailed way.

For more information on the state of play regarding implementation in the different Member States, the European Contact Group has an online database available at <http://www.8cld.eu>.

Public Interest Oversight Board of IFAC (IPIOB)

1. IPIOB published its [newsletter](#) for July 2018.

International Integrated Reporting Council (IIRC)

1. Wendy McGuinness, Chief Executive of the New Zealand-based think tank McGuinness Institute, recently visited the IIRC offices in London. She brought with [her a number of publications from the Institute's Project ReportingNZ, which looks at Extended External Reporting \(EER\)](#).
2. The Institute of Public Auditors in Germany (Institut der Wirtschaftsprüfer in Deutschland) has released a position paper on the future on corporate reporting, (only available in German). IDW's Matthias Schmidt [shared some insights into their thoughts on the future of reporting for IIRC](#).

Global Reporting Initiative (GRI)

1. A "Practical Guide" to enable companies to better measure and report on their impact on the Sustainable Development Goals (SDGs) was released in August by the GRI and the United Nations Global Compact.

The new publication, [Integrating the SDGs into Corporate Reporting: A Practical Guide](#), helps companies of all sizes to prioritize SDG targets to act and report on, set related business objectives, and measure and report on progress.

2. [Ten recommendations](#) intended to stimulate more investment to help advance the Sustainable Development Goals (SDGs) were published in July 2018 at the SDG Business Forum by GRI, Principles for Responsible Investment (PRI) and the United Nations Global Compact. The recommendations focus on how corporate reporting on the SDGs can best address investors' information needs to help mobilize sustainable finance needed for the achievement of the SDGs. The three entities represent the world's leading organizations in the areas of sustainability reporting, corporate responsibility and responsible investing.

International Forum of Independent Audit Regulators (IFIAR)

1. There have been no significant developments related to audit and assurance to report in the period.

International Organization of Supreme Audit Institutions (INTOSAI)

1. On 18 July 2018, the INTOSAI General Secretariat, in cooperation with the United Nations (UN) and the Permanent Representations of Austria and Canada to the UN, organized a side event in the framework of the High-level Political Forum on Sustainable Development (HLPF). The [roundtable discussion](#) hosted by the Permanent Representation of Austria saw the participation of the Secretary General of INTOSAI, Margit Kraker, high-ranking representatives of Supreme Audit Institutions (SAIs), the UN, governments (ambassadors) and representatives of the civil society and national parliaments. The event focused on the results achieved in the framework of auditing the preparedness of national governments to implement the Sustainable Development Goals (SDGs). The stimulating discussions provided vital insights into the various approaches of SAIs in auditing the implementation of the SDGs.

International Organization of Securities Commissions (IOSCO)

1. There have been no significant developments related to audit and assurance to report in the period.

Australia

The Australian Auditing and Assurance Standards Board (AUASB)

1. Highlights from the June 2018 AUASB meeting include:
 - AUASB Members approved the release of an Explanatory Guide for EDs 01/18, 02/18, related to ASA 315 *Identifying and Assessing the Risks of Material Misstatement*; and Eds 03/18 & 04/18, related to ASA 540 *Auditing Accounting Estimates and Related Disclosures*. The Explanatory Guide summarises details of the exposure drafts released by the AUASB in relation to ASA 315 & ASA 540 and details of the change in the due process undertaken for the exposure of ED ASA 315 *Identifying and Assessing the Risks of Material Misstatement*.
 - The AUASB approved the issuance of the EDs for ASA 315, subject to a number of changes that were requested by AUASB members. These changes primarily relate to Explanatory Memorandum and the questions stakeholders should respond to when the EDs are released.
 - The AUASB approved the EDs for ASA 540, subject to a revision of the questions stakeholders should respond to relating to the ASA 540 EDs, which will be redistributed for AUASB consideration out of session and then approved by the Chair before being finalised.
 - The closing date for submissions on the EDs relating to ISA 315 and ISA 540 approved by the AUASB will be 15 October 2018. The final EDs and associated documents will be released on the AUASB Website on 6 August 2018. An additional AUASB meeting will be scheduled in late October 2018 to consider stakeholder responses to both EDs and finalise the AUASB's submission to the IAASB in respect of the exposure draft for ISA 315.

Other News from Australia

1. Elizabeth Carson, with colleagues Neil Fargher and Yuyu Zhang, [examined the reporting behaviour of Australian auditors, noting that the trend in issuing going concern opinions \(GCOs\) had not declined after the GFC as it had in other countries](#). They looked specifically at the issuing of GCOs, where auditors state their doubts about a company's ability to be solvent in 12 months' time, and sought to understand which factors influenced the likelihood of any auditor issuing a GCO, including whether these increases could be attributed to pressure from ASIC's inspections.
2. Journalist and former tax inspector Richard Brooks charts the changes in the global accountancy and auditing industry and its underappreciated role in the financial crash of 2008 in this [podcast](#).

United Kingdom

FRC

1. The FRC held a [panel discussion](#) on 18 July 2018 about how corporate governance is evolving to meet the needs of all stakeholders.
2. There is room for improvement in the audit of pension balances and disclosures in company accounts, according to a new report from the FRC, '[The audit of defined benefit pension obligations](#)'. The FRC focussed on the quality of audit of pension balances and related disclosures in 51 of its audit inspections in 2017/18 and found that in almost half, improvement was required in at least one aspect of the audit work, as well as identifying areas of good practice.

Institute of Chartered Accountants in England and Wales

1. Professional scepticism is central to the work of auditors and yet audit regulators and others continue to express concerns that auditors are not sufficiently sceptical. [This report](#) explores what

auditors and other stakeholders think about how it can be enhanced and who is responsible for it. This report is based on a series of interviews with practising auditors, training providers and audit regulators. It sets out the views of those with first-hand experience of real world auditing and dealing with the pressures of deadlines and budgets on the nature of scepticism, who is responsible for it, and what needs to be addressed to improve it.

The Charity Commission

1. Insider fraud is committed by someone involved within your charity, whether a trustee, an employee or volunteer. The National Fraud Intelligence Bureau (NFIB) [has released a national alert highlighting the insider threat from fraudsters and cyber criminals](#).

Association of Chartered Certified Accountants (ACCA)

1. A new report published today by ACCA, [Business models of the future: systems, convergence and characteristics](#), identifies 12 characteristics behind business model design, that are being combined by organisations in different ways to create new sources of value.

United States of America

Public Company Accounting Oversight Board (PCAOB)

1. There have been no significant developments related to audit and assurance to report in the period.

American Institute of Certified Public Accountants (AICPA)

1. There have been no significant developments related to audit and assurance to report in the period.

Center for Audit Quality (CAQ) - (affiliated with AICPA)

1. In this August 2018 comment letter, [the CAQ provides input](#) on a Consultation Paper, "Professional Scepticism - Meeting Public Expectations," from the International Ethics Standards Board for Accountants (IESBA). Emphasizing the importance of professional scepticism and judgment to audit quality, the CAQ's letter offers IESBA four high-level recommendations related to professional scepticism: (1) Create a better understanding of behavioural characteristics, (2) Seek clarity and address ambiguity, (3) Use collaboration to promote action, and (4) Address the expectation gap.

Canada

Canadian Auditing and Assurance Standards Board (CAASB)

1. The Board received an update on the ongoing discussions with regulators and other stakeholders, and staff research on issues related to the application of key audit matter reporting to TSX listed entities, with a specific focus on investment funds. The Board will continue to discuss these issues at a future meeting.
2. The Board unanimously approved the Canadian exposure draft of revised CAS 315, Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment and conforming amendments. The exposure draft is based on the International Auditing and Assurance Standards Board's (IAASB's) exposure draft of proposed revisions to International Standard on Auditing (ISA) 315, with no proposed Canadian amendments. The exposure draft is expected to be issued in early September 2018, with a comment deadline of November 2, 2018. The Board also discussed the communication and outreach plan related to the exposure draft. English and French webinars will be conducted to build awareness of the

exposure draft. The requirements will be field tested to better understand the practical implications of the proposed revisions. Staff will also be holding several video conferences in September to hear stakeholders' views on the exposure draft.

CPA Canada

1. There have been no significant developments related to audit and assurance to report in the period.

Project	Overview of the project and its current status
<p>Quality Control No Update for the period</p>	<p>Objective of the Project: Initial activities in scoping the project will focus on whether there is a need to revisit specific aspects of the quality control standards to enhance clarity and consistency of their application. This may include restructuring ISQC 1, additional requirements or guidance within the standard or additional guidance in support of the standard. Specific aspects within ISQC 1 and ISA 220 being explored include, governance, engagement partner responsibilities, engagement quality control reviews, monitoring, remediation, alternative audit delivery models and specific issues pertaining to small- and medium-sized practices</p> <p>Background and current status: The proposed changes to QC were included in the IAASB Audit Quality ITC. The ITC response period is closed now. From May to September 2016, the various Working Groups analysed the comment letters to the Overview and detailed ITC, reviewed feedback from outreach activities, and developed project proposals for quality control that were presented at the September 2016 IAASB meeting.</p> <p>The IAASB considered the Quality Control Other Working Group's (QCOWG) proposals in respect of:</p> <ul style="list-style-type: none"> • Setting the objective of an engagement quality control (EQC) Revising the definition of an EQC review; • Determining the scope of the engagements subject to an EQC review; and • The execution of an EQC review. <p>At its March 2017 meeting, the IAASB discussed matters to do with the eligibility of the engagement quality control reviewer.</p> <p>QC-Firm Level</p> <p>In June 2017 the Board discussed the Quality Control Task Force's (QCTF) recommendations on the possible revisions to ISQC 1, a result of incorporating a quality management approach (QMA) into ISQC 1, that included a discussion of a working draft of ISQC 1 (Revised) and how the proposals are expected to change firm behaviors. The Board was supportive of the overall direction proposed by the QCTF and emphasized the importance of outreach with a variety of stakeholders to seek input on the practicality of the proposals. The Board also encouraged the QCTF to develop guidance and examples to accompany the revised standard in order to explain the implementation and application of the standard.</p> <p>In its September 2017, the Board discussed the Quality Control Task Force's (QCTF) recommendations on the possible revisions to ISQC1 in relation to documentation of the system of quality management. The Board was supportive of the QCTF's proposals and suggested various refinements. Some of the key proposals were as follow:</p> <ul style="list-style-type: none"> • the proposal to retain the requirement for an EQC review for all audits of financial statements of listed entities, i.e., not only for general purpose financial statements

	<ul style="list-style-type: none"> • the proposals in relation to other engagements for which the firm determines that an EQC review is required (see here for details) • the objective of ISQC 2, including whether it is appropriate to locate the responsibilities of the EQC reviewer in ISQC 2, instead of ISA 220 • the IAASB supports the proposal to remove the reference to “team” from the definition of an EQC reviewer, and instead explain the use of a team in the application material supporting the appointment of the EQC reviewer • the proposed requirements and application material in relation to the eligibility of the EQC reviewer. <p>The Board also discussed the QCTF’s recommendations in relation to EQC reviews that would be incorporated in ISQC 1 and the proposed new standard, ISQC2. The Board confirmed that the purpose of the EQC review is to evaluate the significant judgments made by the engagement team. In addition to various recommendations to further enhance and clarify the various requirements and application material, the Board encouraged the QCTF to improve the robustness of the requirement relating to the scope of the engagements subject to EQC review.</p> <p>Quality Control – Engagement Level</p> <p>In December 2017, The IAASB supported the direction of the proposed changes to ISA 220.4 In particular, the Board supported the proposed changes that emphasize that the engagement partner is responsible and accountable for audit quality. The Board encouraged the ISA 220 Task Force to consider, as it progresses revisions to ISA 220, how the proposed changes will strengthen the performance of quality audits.</p> <p>Quality Control – Firm Level</p> <p>In December 2017, the Board discussed a first read of the proposed exposure draft of ISQC 1 (Revised) 5 and was broadly supportive of the direction of the standard. The Board focused on the scalability of the standard, clarifying the interrelationship of the components, and the appropriate placement of the governance and leadership component. As well as requesting the Task Force to clarify the meaning of deficiencies and major deficiencies, the Board asked that a framework be developed for assessing deficiencies in the system of quality management and requested clarification of how such deficiencies may impact the achievement of the overall objective of the standard. The Board also asked the Task Force to reconsider the threshold for the identification of quality risks and encouraged the Task Force to explore the development of appropriate guidance to accompany the proposed exposure draft that addresses the application of the standard to a spectrum of firms.</p> <p>The Task Force will continue to progress the proposed changes to the standard for a second read of an exposure draft in March 2018.</p>
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<p>Group Audits– ISA 600</p> <p>No Update for the period</p>	<p>Objective of the project: Determining the nature of the IAASB’s response to issues that have been identified, relating to Group Audits, from the ISA Implementation Monitoring project and outreach activities, inspection reports from audit regulators, discussion with NSS and responses to the IAASB’s Work Plan consultation (i.e., whether standard-setting activities are appropriate to address the issues, and if so, whether specific enhancements within ISA 600 or a more holistic approach to the standard would be more appropriate).</p> <p>Background and current status: The IAASB commenced work on one aspect of this project relating to the responsibilities of the engagement partner in circumstances where the engagement partner is not located where the majority of the audit work is performed in December 2014. A Staff Audit Practice Alert on this aspect was published in August 2015. Information gathering on the broader aspects of group audits commenced in March 2015.</p> <p>The issues identified and discussed at the IAASB meetings form part of a combined Invitation to Comment on Enhancing Audit Quality in the public interest which was issued in December 2015 and is open for comments till May 16, 2016. The ITC is now closed. From May to September 2016, the various Working Groups analysed the comment letters to the Overview and detailed ITC, reviewed feedback from outreach activities, presented the results to IAASB at the September 2016 IAASB meeting.</p> <p>In its June 2017 meeting, the IAASB received an update on the activities of the GATF. The IAASB supported the proposal of the GATF to engage more directly with the QCTF, ISA 220 TF and ISA 315 (Revised)3 TF, to help ensure that the requirements in those standards provide appropriate connection points between those projects and ISA 600.4 The IAASB also supported the proposal of the GATF to publish a short project update and asked the GATF to consider topics that are related to standards not under revision, for example, materiality and audit evidence.</p> <p>In December 2017, the Board received a presentation about the interconnections between ISA 600 and other ongoing projects, and how the Task Force is monitoring the activities of the other task forces, providing input and considering implications of changes in the other standards on ISA 600.</p>
<p>Professional Scepticism</p> <p>No Update for the period</p>	<p>Objective of the project: To make recommendations on how to more effectively respond to issues related to professional scepticism.</p> <p>Background and current status: The IAASB commenced its initial information gathering on the topic of professional scepticism in June 2015. The issues identified and discussed at the IAASB meetings are part of the Invitation to Comment on Enhancing Audit Quality in the Public Interest which was issued in December 2015 and is open for comments till May 16, 2016.</p> <p>The working group is comprised of representatives from the IAASB, the International Ethics Standards Board for Accountants (IESBA), and the International Accounting Education Standards Board (IAESB) to explore the topic of professional scepticism, enabling the three independent standard-setting Boards to consider what actions may be appropriate within their collective Standards and other potential outputs to enhance professional scepticism.</p>

	<p>Together with the Quality Control and ISA 600-Group Audits project, this project is part of the Audit Quality Enhancements Coordination Group (AQECG). The AQECG intends to coordinate the various inputs to the invitation to comment developed at the individual working group level, and take a holistic approach as to how the matters are presented in one invitation to comment. From May to September 2016, the various Working Groups analysed the comment letters to the Overview and detailed ITC, reviewed feedback from outreach activities, presented the results to IAASB at the September 2016 IAASB meeting.</p> <p>Subsequent to the December 2016 IAASB meeting, the joint PSWG held a teleconference to discuss matters related to potential changes to the concept/definition of professional scepticism in the ISAs. The March meeting papers are available here.</p> <p>In June 2017 meeting, the IAASB received an update on the activities of the Professional Skepticism Working Group (PSWG) and the Professional Skepticism IAASB Subgroup since the last Board meeting in March 2017. The Board supported the release of a communication to update stakeholders about the actions and current status of the PSWG's work. The Board also discussed the concept of "levels" of professional skepticism and supported the recommendations of the Professional Skepticism IAASB Subgroup not to introduce the concept into the ISAs.</p> <p>The IAASB discussed the Professional Skepticism Subgroup's analysis and related conclusions regarding different "mindset" concepts of professional skepticism and the use of the words in the ISAs in its December 2017. The Board supported the conclusions of the Subgroup, including that the current concept of the attitude of professional skepticism involving a "questioning mind" continues to be appropriate and should be retained within the ISAs. The IAASB Professional Skepticism Subgroup will liaise as needed with the Professional Skepticism Joint Working Group.</p>
<p>Accounting Estimates (ISA 540) and Special Audit Considerations Relevant to Financial Institutions (No Update for the period)</p>	<p>Objective of the project: The objective of the financial institutions project is to:</p> <ul style="list-style-type: none"> A. Clarify and enhance the relationship between the banking supervisors and the bank's external auditors; B. Consider and address issues of particular significance in audits of financial institutions; and C. Consider as to whether the issues relating to ISA 540 that have been highlighted as particularly relevant to audits of banks and other financial institutions are more broadly applicable to other entities <p>Background and current status: The ISA Implementation Monitoring project, specific requests from banking and insurance regulators and outreach activities by the ISA 540 Working Group, have identified issues with respect to auditing accounting estimates, in particular in relation to audits of financial institutions. Also, inspection finding reports from audit regulatory bodies highlighted consistent issues with respect to the audit of accounting estimates, including in relation to audits of financial institutions. There are areas where there have been calls for clearer or additional requirements or guidance to enable auditors to appropriately deal with increasingly complex accounting estimates and related disclosures, including obtaining sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements as a whole.</p>

	<p>A draft exposure draft of revised ISA 540 has been developed and is to be deliberated by IAASB with an approved ED expected to be issued for comment in December 2016. The board reviewed the draft in its June 2016 meeting.</p> <p>IAASB expects to complete its deliberation of responses to the exposure draft and resulting proposed changes to ISA 540 (Revised) in 2017 with the revised standard expected to be issued in last quarter of 2017.</p> <p>The IAASB has released the ED ISA 540 for comment in May 2017.</p> <p>The Board received an overview of the comment letters received on proposed ISA 540 (Revised) in its September 2017 meeting. The Board discussed respondents' concerns about the complexity of the proposed ISA and potential difficulties in understanding and applying it in practice, and asked the ISA 540 Task Force to look at ways to restructure the proposed ISA to improve its clarity and readability. The Board also discussed the scalability of the ISA, how risk factors could be taken into account, and how best to structure the response to the assessed risks of material misstatement. The Board highlighted the importance of achieving the right balance between issuing a high-quality standard and the public interest in finalizing the ISA in a timely fashion. The IAASB is holding an additional meeting in October to progress proposed ISA 540 (Revised).</p> <p>The IAASB discussed key issues raised by respondents in relation to the Exposure Draft of ISA 540 (Revised), Auditing Accounting Estimates and Related Disclosures', including the scalability of the ISA, the use of the term "reasonable," the exercise of professional skepticism and the Task Force's approach to the application material. The IAASB also discussed the Task Force's revisions to requirements and application material based on comments received on the Exposure Draft. The IAASB asked the Task Force to focus on redrafting the application material according to the planned approach with a view to conducting a first read of ISA 540 (Revised)¹ in March 2018, ahead of a targeted approval in June 2018.</p> <p>The ISA (540) was approved in IAASB's June 2018 meeting.</p>
<p>Data Analytics</p> <p>No Update for the period</p>	<p>Objective of the project: The objective of the Data Analytics Working Group (WG) is to:</p> <ul style="list-style-type: none"> A) Explore emerging developments in audit data analytics; and B) Explore how the IAASB most effectively can respond via International Standards or non-authoritative guidance (including Staff publications) and in what timeframe. <p>Background and current status: Information gathering on data analytics began in April 2015 and the Data Analytics Working Group will continue with its planned outreach activities in future. The DWAG published its first publication "The IAASB's Work to Explore the Growing Use of Technology in the Audit" in June 2016.</p> <p>At the March meeting, the IAASB received a video presentation of a panel discussion among members of the DAWG that was presented at the International Forum of Independent Audit Regulators Inspections Workshop.</p>

	<p>The Chair of the DAWG provides an update on the project in February 2017 on the IFAC website.</p> <p>In its June 2017 meeting, the IAASB received a presentation of high-level observations from respondents to the IAASB's Request for Input: Exploring the Growing Use of Technology in the Audit, with a Focus on Data Analytics. It was noted that respondents supported the IAASB in undertaking this work and encouraged continued active participation of the Data Analytics Working Group in other current standard-setting projects of the IAASB underway.</p>
<p>Emerging External Reporting Update for the period No the</p>	<p>Objective of the project: The objective of the Integrated Reporting Working Group (IRWG) is to:</p> <ul style="list-style-type: none"> A) Explore emerging developments in integrated reporting and other emerging developments in external reporting; B) Gather further information on the demand for assurance, the scope of the assurance engagement and the key assurance issues; and C) Explore how the IAASB most effectively can respond via International Standards or non-authoritative guidance (including Staff publications) and in what timeframe. <p>Background and current status: At its September 2014 meeting the Innovation WG proposed, and the IAASB agreed to establish a WG to specifically monitor the developing interest in integrated reporting and the demand for assurance on integrated reports. This includes initial thinking on the nature of such engagements, including the scope of the assurance engagement, the suitability of the criteria, and other matters related to assurance on integrated reports. The Board considered the draft working paper prepared by the IRWG Supporting Credibility and Trust in Emerging Forms of External Reporting in its June 2016.</p> <p>The Discussion Paper was issued in August 2016.</p> <p>In its June 2017 meeting, the IAASB received a presentation about the high-level observations from the comment letters received to the Discussion Paper, Supporting Credibility and Trust in Emerging Forms of External Reporting. It was noted that respondents generally supported the development of guidance on how to apply existing international assurance standards rather than developing new standards, and that the IAASB should continue to provide thought leadership on assurance issues and coordinate its work with other relevant organizations.</p> <p>The Board received an update on the project in December 2017. It was noted that the grant agreement with the World Business Council for Sustainable Development (WBCSD) was finalized for the funding of the project and that the Project Proposal and Feedback Statement has been finalized to be published on the IAASB's website. The board also received an update on the plan for developing the framework for the non-authoritative guidance for EER during the next year, including the required research to be gathered and the establishment of a Project Advisory Panel (PAP).</p>

<p>Agreed-Upon Procedures</p> <p>No Update for the period</p>	<p>The objective of the project is to:</p> <p>A) Revise International Standard on Related Services (ISRS) 4400, Engagements to Perform Agreed-Upon Procedures Regarding Financial Information in the Clarity format; and</p> <p>B) Consider whether standard-setting or other activities may be appropriate for engagements that use a combination of procedures derived from review, compilation and agreed-upon procedures engagements (also known as "hybrid engagements"), in light of the existing standards that may be applicable to these services in the IAASB's current suite of standards.</p> <p>Background and current status: During consultations on the IAASB's 2015-2019 Strategy and the related 2015-2016 Work Plan, many stakeholders expressed the need to revise ISRS 4400 to meet the growing demand for agreed-upon procedure engagements. In response to the stakeholders' comments, the IAASB established a working group to explore issues involving agreed-upon procedure engagements. The issues identified and discussed at the IAASB meetings will be used to revise ISRS 4400 and possibly develop new standard(s) or guidance that would address engagements where there is a combination of agreed-upon procedures and assurance.</p> <p>The Agreed-Upon Procedures (AUP) Working Group presented a first draft of its Discussion Paper, <i>Exploring the Growing Demand for Agreed-Upon Procedures Engagements and Other Services and the Implications for the IAASB's Standards</i>, to the Board in June 2016. The IAASB provided the AUP Working Group with input to enhance the Discussion Paper and suggested that the paper pose a question to explore whether the IAASB should develop guidance on multi-scope engagements. The AUP Working Group will present a revised draft of the Discussion Paper at the September 2016 IAASB meeting.</p> <p>In its September 2017 meeting, the Board discussed the feedback received on the Discussion Paper and approved a standard-setting project proposal to revise ISRS 4400, subject to clarifications around the use of judgment, independence, restriction of the report of factual findings and required documentation.</p>
<p>ISA 315 (Revised) (has update for the period)</p>	<p>The tentative objectives of the projects at this stage are:</p> <p>A) to address the issues that have been identified by the ISA Implementation Monitoring project.</p> <p>B) Possible changes that may be necessary to ISA 315 (Revised) to enhance the requirements and guidance for evolving environmental influences (such as changing internal control frameworks and more advanced technology systems being utilized by both management and auditors).</p> <p>C) In its June 2016 meeting, the IAASB directed the ISA 315 (Revised) Working Group to present a project proposal for the IAASB's consideration at its September 2016 meeting to commence standard-setting activities. The <u>project proposal</u> was presented and approved in the IAASB's September 2016 meeting.</p> <p>Since the December 2016 IAASB meeting, the task force has had one physical meeting and two teleconferences to develop the <u>March meeting papers</u>.</p>

	<p>In September 2017, the ISA 315 Task Force presented proposed changes to the requirements in ISA 315 (Revised) to address identified issues relating to understanding the entity and its environment, including the applicable financial reporting framework, and internal control, including obtaining an understanding of the five components of internal control. The Board broadly supported the proposals, but asked for consideration about some of the proposed changes to the definitions, as well as the perceived focus on controls in obtaining the necessary understanding of the components of internal control. With regard to proposed changes to the identification and assessment of inherent and control risk, the Board supported a separate assessment of inherent and control risk, but asked that the ISA 315 Task Force further consider how this works practically and highlighted that further clarification is needed relating to the assessment of control risk.</p> <p>In December 2017, the Board discussed a first read of proposed changes to the requirements and application material of ISA 315 (Revised)². The Board broadly supported the proposals, but asked for further consideration by the Task Force on various matters, including aspects of the definitions of 'controls' and 'relevant assertions,' and regarding the introduction of the term 'business model' and its interactions with current requirements of the standard. The Board also questioned the use of 'sufficient and appropriate' as it relates to potential confusion with "sufficient appropriate audit evidence" and whether a change may have unintended consequences if this concept were to be introduced as proposed. The Board encouraged further consideration about how fraud can be included as a qualitative inherent risk factor, taking into account how this would link to the fraud risk factors in ISA 240.3 The Board continued to be supportive of the introduction of "spectrum of risk" but thought the spectrum of risk could be better emphasized and explained earlier in the standard.</p> <p>The Board recognized the need for further consideration about scalability, but agreed that scalability should be presented through the requirements and application material in context of the auditor's consideration of risk thereby eliminating the need for "considerations for smaller entities."</p> <p>The Task Force will continue to progress the proposed changes to the standard for a second read of an exposure draft in March 2018.</p> <p>Update for the period</p> <p>The ED was issued in July 2018 for public consultation.</p> <p>Please refer agenda item 5.1</p>
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NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

DATE: 24 August 2018

TO: Members of the New Zealand Auditing and Assurance Standards Board

FROM: Peyman Momenan

SUBJECT: Domestic Update

Introduction

1. This Update summarises the significant news from Financial Market Authority, New Zealand Institute of Chartered Accountants and other organisations for the Board's information, for the period July and August 2018.

Financial Markets Authority (FMA)

1. The FMA has released its [annual corporate plan](#) as the conduct and culture of New Zealand's financial services industry comes under greater scrutiny.
2. Confidence in New Zealand's financial markets has remained stable since 2017, despite uncertainty around a potential trade war, volatile global markets and a focus on the culture and conduct of major financial institutions in Australia and New Zealand. The Financial Markets Authority today released [its annual survey into the public's attitude to financial markets](#).

The New Zealand Institute of Chartered Accountants

1. The CA ANZ has published the following to articles as part of its Perspective series:
 - [Limited scope consultation on the audit of service performance information](#) (written by Misha Pieters for CAANZ)
 - [Reform of international auditing and assurance standard setting](#)

CPA Australia

1. There have been no significant developments relating to audit and assurance to report in the period.

The Institute of Directors (IoD)

1. There period have been no significant developments relating to audit and assurance to report in the.

Sustainability Matters

1. The start of a conversation on improving the risk management and resilience of the Living Standards Capitals. "This paper is one of a series of Discussion Papers on wellbeing in the Treasury's Living Standards Framework (LSF). The papers on the relationship between the LSF and the Sustainable Development Goals, Financial/Physical Capital, and the note on the role of culture in the LSF are all Discussion Papers. The Discussion Papers are not the Treasury's position on measuring intergenerational wellbeing and its sustainability in New Zealand. Our intention is to encourage discussion on these topics. "There are marked differences in perspective between the papers that reflect differences in the subject matter as well as differences in the state of knowledge. The Treasury welcomes comments on these papers to help inform our ongoing development of the Living Standards Framework.

Review of the Charities Act 2005

1. The Minister for the Community and Voluntary Sector has announced a review of the Charities Act 2005. The Policy Group of the Department of Internal Affairs will be leading the review, and the Minister will be the key decision maker.

More information can be found [here](#) , including the Terms of Reference.

Other matters of interest

1. Appendix 1 includes the interview with Institute of Business Ethics director Philippa Foster Back on Carillion collapse and ethical and other lessons for New Zealand.

Appendix 1: NBR article re Carillion collapse and ethical and other lessons for New Zealand

The UK's second-largest construction group collapsed in January under a £1.5 billion debt pile.

Carillion's rise and spectacular fall was summed up by a report of the House of Commons business, energy and industrial strategy and work and pensions committee as a "story of recklessness, hubris and greed" and its business model as an "unsustainable dash for cash."

"The mystery is not that it collapsed but how it kept going for so long," the report said.

Even as the company began to publicly unravel, the board was concerned with increasing and protecting generous executive bonuses.

Why should New Zealanders care about a failed company on the other side of the world?

For one thing, an official report on the collapse showed there were fundamental flaws in the way the government awarded contracts because of an aggressive approach to risk transfer to drive down the cost of providing public services. Carillion had won contracts for the UK National Health Service and the Ministry of Defence, was a central contractor on a major rail project, repaired some prisons, and provided cleaners and caterers to schools.

That issue of undue risk being placed on contractors, particularly under government contracts, has been raised by New Zealand's construction industry and blamed for some well-publicised company losses or failures here, including Ebert Construction last month.

Salutory lesson

But the biggest lesson from Carillion is one of ignoring culture and ethics at your own peril, says Philippa Foster Back, the director of the UK-based Institute of Business Ethics.

She was also a minor shareholder in Carillion and among those affected by its collapse.

The House of Commons report noted corporate culture doesn't emerge overnight, and that the chronic lack of accountability and professionalism now evident in Carillion's governance

were failure years in the making.

"The board was either negligently ignorant of the rotten culture at Carillion or complicit in it," it said.

The report also said investors who sought to discuss concerns about management failures were met with unconvincing and incompetent responses.

"Investors were left with little option other than to divest," she says.

Her key message at the recent NZ Shareholders' Association conference was that shareholders need to stop thinking of just short-term dividends and think more broadly about the longevity of the quality of a company's bottom line.

“The way companies are running themselves, if they have a good culture, an open culture, there is a lot of evidence to suggest that will feed through to the bottom line because people enjoy working there.”

Culture is an under-estimated aspect of business, which has only really come to the fore in the UK in the past few years.

Listed companies are covered by corporate governance codes but until now there has been little oversight, over than legal requirements, of the way large private companies are run.

In the wake of some corporate scandals and decline in public trust of how big business operates, the UK government set up a committee which has just reported back on suggested voluntary corporate governance principles for private companies.

Ms Foster-Back, who was involved in setting the principles being consulted on before implementation next year, says they will be useful to “give people comfort that you’re mindful of not just your bottom line but also how you do business.”

The Kiwi view

An institute survey released late last year of New Zealand chief executives’ perspective on ethical business leadership found while there was an increasing appreciation of its importance, most felt there was little to worry about in this country.

Ms Foster-Back says what came out was that New Zealand companies are not as far advanced as some other countries in having mechanisms to take ethical values and bring them alive for staff.

“There is a natural feeling that New Zealand is a good country to do business in and that there is a very high level of honesty,” she says. “But there are quite a number of underlying issues, it’s a small country and therefore has potential conflicts of interest and things like that do need to be aired.”

A recent Ethics at Work 2018 survey carried out in Europe by the institute found one in three employees were aware of some misconduct in the workplace while one in six had felt some form of pressure to compromise their organisation’s ethical standards. More were likely to speak up about conduct at work than when in the last survey in 2015.

The most frequent problems in any country are abusive bullying, harassment and not treating staff well.

The same study is now being conducted in New Zealand on employees’ attitudes to ethics in the workplace and Ms Foster Back is expecting similar outcomes to the European survey once it is published in November.

Key indicators of corporate culture

Ms Foster Back says its important for investors and boards to look beyond the ethics, values and beliefs a company says it has and probe what it is actually doing. The institute would like to see a list of standardised cultural indicators companies should report on annually but in the interim has compiled a list that can be checked relatively easily.

To: NZAuASB members
From: Rowena Sinclair
Date: 23rd August 2018
Re: Academic update 2018-5

This fifth update for the year focuses on three items that are on the International Auditing and Assurance Standard Board (IAASB)'s agenda: (1) data analytics; (2) accounting estimates or fair value accounting; and (3) group audits.

(1) DATA ANALYTICS

Big data characterises data that has large variety, high velocity, and potentially unlimited volume. The authors consider that this data could originate from sources unfamiliar to many auditors e.g. *"videos, audio files, tweets, social media"* (Appelbaum, Kogan & Vasarhelyi, 2017, page 4).

Appelbaum, et al. (2017, page 2)'s article provides a timely overview of big data and the issues facing auditors, and details six concerns:

1. *Should new (modern) analytics methods be used in the audit process?*
2. *Which of these methods are the most promising?*
3. *Where in the audit are these applicable?*
4. *Should auditing standards be changed to allow/facilitate these methods?*
5. *Should the auditor report be more informative?*
6. *What are the competencies needed by auditors in this environment?*

(2) ACCOUNTING ESTIMATES/FAIR VALUE ACCOUNTING

The IAASB approved International Standard on Auditing 540 Auditing Accounting Estimates, including Fair Value Accounting Estimates, and Related Disclosures (ISA 540) at the IAASB's June 2018 meeting.

The issue of fair value accounting has been covered in several academic papers that provide an overview of some of the issues auditors grapple with when faced with accounting estimates.

First, an interesting historical study by Haswell & Evans (2018, page 25) who found links between *"the collapse of Enron and adjustments to fair value accounting in the mid-2000s, which in turn became implicated in the global financial crisis"*. Their overall conclusion is of lessons not learned so that history repeated itself.

Smith-Lacroix, Durocher & Gendron's (2012, page 51) Canadian study interviewed 18 audit partners/managers and highlighted the uncertainty in financial statements reflected by the following interviewee:

"All we should have to do is present fair value within an acceptable range and state that fair value is somewhere between such and such amount, according to the estimates."

The study also identified the *"high degree of dependence towards valuation expertise"* when accounting estimates are involved (Smith-Lacroix et al., 2012, page 50). Cannon & Bedard's (2017, page 81) study considered the impact of using a valuation specialist in more depth and found that *"procedures performed by specialists have the highest yield in identifying problems"* by the auditors and clients.

Joe, Vanderveide & Wu's (2017, page 110) study found that:

"Auditors' preference for well-defined tasks that are lower in ambiguity and more verifiable motivated them to attend to quantitative evidence and diverted audit effort away from testing qualitative evidence, such as subjective audit procedures that test the discretionary aspects of the client's FV estimate".

(3) GROUP AUDITS

Sunderland and Trompeter's (2017) paper provide a useful analysis of the areas of concern from the IAASB's post-implementation review of its clarified standards and noted two major categories of ongoing contention in group audits:

- A. The nature and extent of group auditor involvement particularly:
 - 1. Knowledge of the component;
 - 2. Understanding the component auditor and staffing the global engagement team;
 - 3. Documentation and communication between group and component auditors;
 - 4. Workpaper review; and
 - 5. Specification / communication of risks.
- B. Materiality and scoping

Graham, Bedard & Dutta (2017, page 40) offer a:

"practical step-by-step method for determining a minimum number of component audits needed to support an aggregate low level of audit risk of material misstatement".

Their method [summarised below] considers risk from components not audited, and the paper provides three illustrations of this method.

- A. Preliminary steps
 - 1. Assessing risk
 - 2. Identifying individual large, high-risk, and insignificant sites
 - 3. Targeting an acceptable level of overall risk: setting selection and detection risk
- B. Determination of a surrogate measure for selection
- C. Considering possible patterns of misstatement.

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